Macro Weekly

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Last week

- **The War/European Energy/Commodities**
  - The war goes on, and on, and on
  - **European natural gas & electricity prices** fell further last week, as gas inventories are approaching is highest level ever (for mid January). The front end contracts are lower than before the war started – but the rest of the curve is still above, but has been lowered by up to 50% the recent weeks
  - The **oil price** rose significantly, we assume due to hopes for an imminent recovery in China (it is probably underway), and less need for monetary tightening (and a recession) in US (and other DMs) as inflation no doubt is heading down
  - The same goes for **iron ore and metals prices** in general – but **food prices** fell again, even measured in a 2% weaker USD
- **Global Auto Sales**
  - **Global auto** sales fell by some 1% in December, and are 8% below the 2019 level. China, US, UK, India and Japan contributed on the downside in December, while sales in the EMU continued upwards as German sales 'exploded' (albeit not as impressive as Norwegian sales). Last year, global auto sales were unchanged vs. the 2021 level but sales are still down 11% vs. the 2019 level – and 21% below the 2018 level! Chinese sales rose by 10% from the 2019 level, India was up 11%, while US was down 19%, and EMU & UK sales were down 29%. (Sweden is down 20%, Denmark 34% - and Norway is <u>up</u> 19%)
- **China**
  - **Mobility** is very likely surging, as road congestion is back to a normal level and number of metro passengers is on the way back too. It seems likely that the full-blown Covid wave with a rather mild virus variant with an extreme high reproduction number (remember the R??) – perhaps at 16 in a population with low immunity – took some very few weeks to blow through most of the population. It is reasonable to expect <u>some very strong growth numbers the coming months</u>, especially retail sales – both in retail trade, services, tourism included
  - **Exports** stabilised in December, following the rapid decline in October and even more in November. Exports are down 10% y/y, 2 pp less than expected. During the pandemic, Chinese exports have been record strong, supply chains have been excellent (by and large), and exports have just fallen down to the pre-pandemic trend recent months. **Imports** rose slightly in December, but import volumes remain below the pre-pandemic trend (even if the level is higher), no doubt due to weak domestic demand. We expect <u>imports to increase rapidly the coming months as domestic demand will increase substantially</u>, at least private consumption. The recent decline in exports are very likely at least partly is due to the fruitless zero-tolerance Covid policy, and the impact of the infection surge from early December, a partial recovery in exports is likely too
  - **Credit growth** was modest in December too, and the Covid surge may be an explanation – but it may also be that the authorities so far have not have been able reignite the animal spirit in the credit market (or in the real estate sector). Even if underlying credit growth is running at some 7% (and down from well above 10% in early 2022), the growth rate is not low at all, and authorities will very likely not want to accelerate credit growth by much as they are well aware of the 'credit bubble risk'. Still, now a growth recovery is at the top of the agenda…
  - Over the past few weeks, Chinese authorities have made **several political turnarounds**, which few thought was likely when president Xi took full control over the CCP in October, and signalled a 'left' turn. The Covid policy was ditched, the crackdown in Big Tech more or less brought to an end, economic stimulus has been promised, including more support for the ailing construction sector. More critical comments vs. Russia's war in Ukraine, and a less aggressive tone vs. US and the West, adds to the possible political shift, which may have substantial economical consequences. If it is for real

Last week II

- **USA**
  - **Headline CPI** inflation fell 0.6 pp to 6.5%, as expected, while the core rate retreated by 0.3 pp to 5.7%, also as expected. Energy prices fell m/m, as did core goods prices (for the 3rd month in row!), and food price inflation is slowing. Housing rent inflation is still accelerating, up to 7.7%, and contributes by 3.2 pp to the core rate! Inflation is new leases is slowing, and at one stage rent inflation in the CPI will slow as well. Core services x housing is up 6.2% y/y, but monthly increases may now be slowing somewhat.
  - The share of SMEs that **plan to hike prices** the coming months nosedived in Dec, almost down to an average level, according to the **NFIB survey** signalling a further slowdown in monthly (and annual) increases in the CPI. Other surveys have also reported a rapid decline in price increases
  - Annual growth in the **Atlanta Fed's median wage tracker** slowed by 0.3 pp to 6.1% in December and has very likely peaked. The labour market is probably marginally less tight, at least measured by the no. unfilled vacancies, fewer companies report they are unable to fill positions. Still,
  - **Taken together**, no doubt good news on inflation – perhaps even wage inflation. The latter is the most important for the Federal Reserve – and even if wage inflation very likely has peaked, wage inflation is well above a level that will yield 2% CPI inflation over time (barring a continued decline in profit margins). Without a far less tight labour market, we still doubt wage inflation will come down sufficiently. Anyway, markets enjoyed the CPI & wage news, understandingly. Another Goldilocks week, even if 10 y rate in the US fell just 6 bps, to 3,49%. In Europe, rates fell much more, Norway included
- **EMU**
  - **Unemployment** is still on the retreat, and the number of unemployed persons fell again in December, by 2', but the unemployment rate was unchanged at 6.5%. Vacancies have peaked, but are still high, and there are no clear signs of a cooling of the labour market yet
  - **Industrial production** gained is expected up 0.5% in November, following the 2% drop in October
- **Sweden**
  - **GDP** fell in Nov but Q4 will very likely be well above Riksbank's forecast, we assume +0.4% vs. the Bank's -0.8%! (The forecast was made in Nov)
  - **CPI** inflation at 12.3% y/y was 0.3 pp higher than expected, while the core (CPI-F x energy but including food) is up 8.4%. If food is removed, the core is close to 5% - as food prices are up by an incredible 18%!
  - However, not all prices are increasing; Realtors reported a 1.5% decline in **flat prices** in Dec – and they are down 12% from the peak in March
- **Norway**
  - **Headline CPI** inflation fell to 5.9% in December from 6.5% in November, 0.2 pp below consensus but as we assumed – but not exactly for the right reason: core inflation accelerated 0.1 pp to 5.8% (up 0.5% m/m), 0.1 pp more than expected but 0.3 pp above our forecast, while energy prices were even lower than we assumed. Imported goods (PC/TVs, household textiles, cell phones) contributed the most but domestically goods and services rose 0.3% m/m – and the domestic component contributes more (3.3 pp) to annual growth in core CPI than imported goods (2.3 pp). BTW, the core ex food is at 4.8% - and accelerating
  - **Mainland GDP** grew by 0.2% in November, in line with consensus (our f'cast was 0.4%), but above Norges Bank' s 0.3% decline, and October was revised slightly upwards. GDP growth has once again remained stronger than NoBa has expected, but that by itself is not an argument to raise rates by more than the planned 25 bps in March

The Calendar: China data, Beige Book, US retail sales, housing mkt + NoBa!

Time	Count.	Indicator	Period	Forecast	Prior
Monday Jan 16					
08:00	NO	Trade Balance	Dec		101.1b
Tuesday Jan 17					
03:00	CN	Industrial Production YoY	Dec	0.2%	2.2%
03:00	CN	Retail Sales YoY	Dec	-9.5%	-5.9%
03:00	CN	Fixed Assets Ex Rural YTD YoY	Dec	5.0%	5.3%
03:00	**CN**	**GDP YoY**	**4Q**	**1.6%**	**3.9%**
03:00	**CN**	**GDP QoQ**	**4Q**	**-1.2%**	**3.9%**
06:00	SW	PES Unemployment Rate	Dec		3.0%
08:00	**UK**	**Weekly Earnings ex Bonus**	**Nov**	**6.3%**	**6.1%**
11:00	GE	ZEW Survey Expectations	Jan	-15	-23.3
14:30	US	Empire Manufacturing	Jan	-8.3	-11.2
Wednesday Jan 18					
	JN	BOJ 10-Yr Yield Target	Jan-18		0.00%
08:00	UK	CPI YoY	Dec	10.5%	10.7%
08:00	UK	CPI Core YoY	Dec	6.2%	6.3%
11:00	EU	CPI YoY	Dec F	9.2%	9.2%
11:00	EU	CPI Core YoY	Dec F	5.2%	5.2%
14:30	US	Retail Sales	Dec	-0.8%	-0.6%
14:30	**US**	**Retail Sales Ex Auto MoM**	**Dec**	**-0.5%**	**-0.2%**
14:30	US	PPI Ex Food and Energy YoY	Dec	5.5%	6.2%
15:15	**US**	**Manufacturing Production**	**Dec**	**-0.2%**	**-0.6%**
16:00	US	NAHB Housing Market Index	Jan	31	31
20:00	US	Beige Book			
Thursday Jan 19					
08:00	NO	Industrial Confidence	4Q	(-5)	-4.4
08:00	NO	Housing starts	Dec		
10:00	**NO**	**Deposit Rates**	**Jan-19**	**2.75%(2.75**	**2.75%**
14:30	US	Building Permits	Dec	1370k	1342k
14:30	US	Housing Starts	Dec	1358k	1427k
14:30	US	Philadelphia Fed Business	Jan	-10	-13.8
14:30	US	Initial Jobless Claims	Jan-14	212k	205k
Friday Jan 20					
08:00	UK	Retail Sales Ex Auto Fuel MoM	Dec	0.4%	-0.30%
16:00	US	Existing Home Sales	Dec	3.95m	4.09m

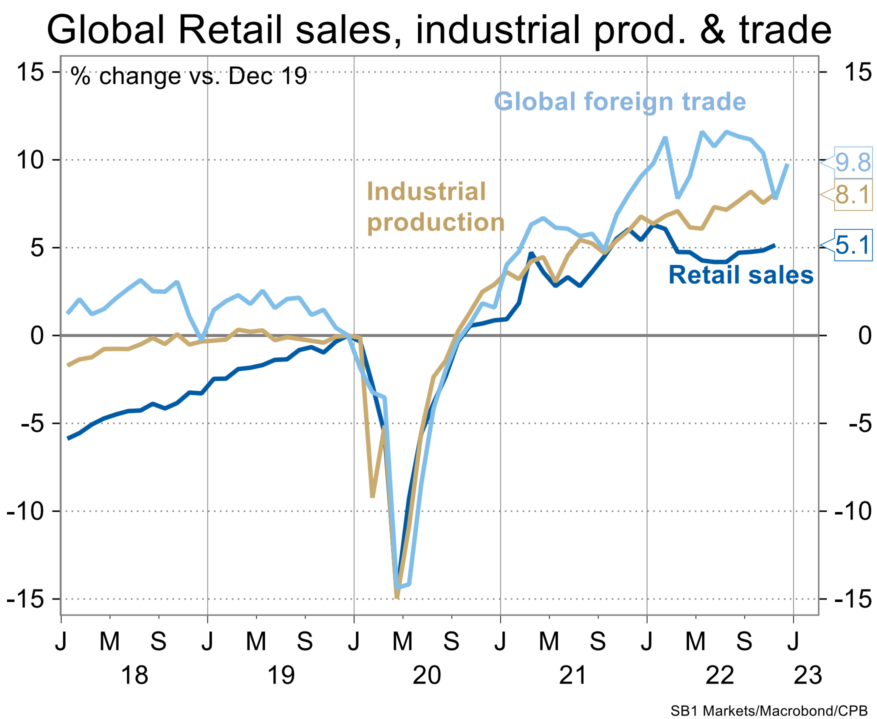
In addition, watch out for outcome of **Bank of Japan's policy meeting** at Wednesday. The zero interest policy may not be ditched but there are intense speculations about a further lifting of the YCC corriodor (now +/-50 bps), and other measures to normalise the Bank's monetary pol.

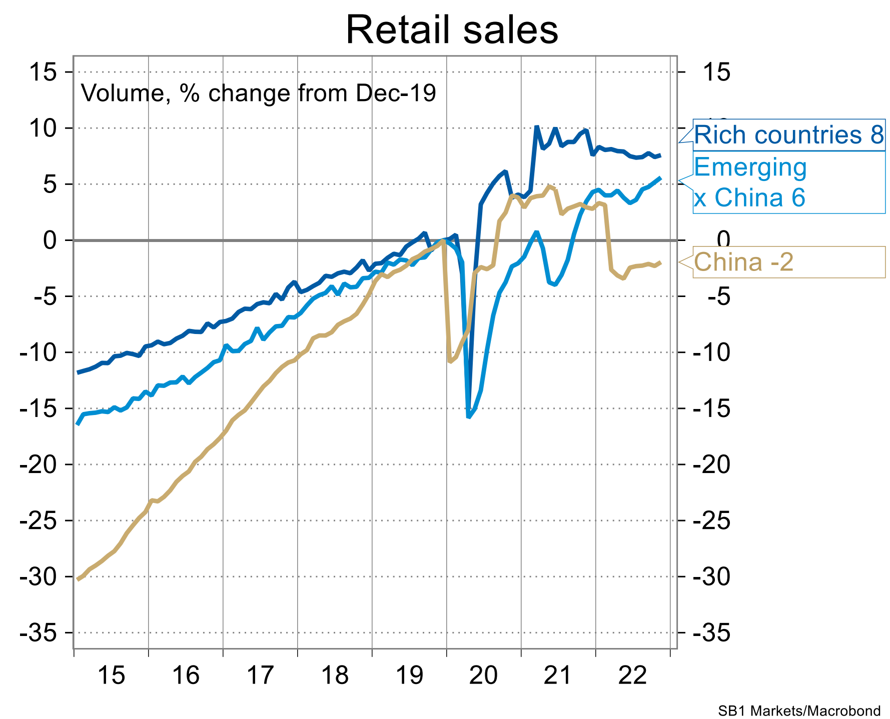
- **China**
  - **GDP** is expected down 1.2% q/q in Q4, reversing the recovery in Q3. The lockdowns in November, and then the negative activity shock in December as they 'all' got infected at once, when corona restrictions were removed will hurt both the Q4 average and very likely December **activity data** – industrial production, retail sales & investments/housing sales & starts which is reflected in the forecasts. However, exports (and imports kept up well in Dec, though compared to a low level in Nov, especially for exports
- **USA**
  - The last Fed's **Beige Book** reported that respondents had grown more pessimistic due to high inflation and slowing demand. Price pressures has eased since then and the economic activity was strong in Q4, but the outlook is probably still deemed to be rather gloomy, as reported by the PMIs/ISMs. We expect more news on easing price pressures, and a marginally less tight labour market
  - Manufacturing production is expected further down in Dec – and the short-term trend is weak. The first January manuf. surveys will also be reported
  - **The housing market** is in a really bad shape, and construction activity/employment will decline substantially in H1. Housing stars are expected further down in Dec
  - **Retail sales** have been remarkably strong recently as households have dipped into their savings in order to keep consumption up, in spite of the decline in real wages. A decline in sales is expected in Dec, also beside the setback in auto sales
- **UK**
  - **Wage inflation** has crossed the 6% line, and there are public sector strikes by the day – where the claims seem to be close to the 10% rate of inflation. This is Bank of England's HUGE challenge
- **Norway**
  - A pause: **Norges Bank** will not hike the signal rate from 2.75% at this meeting. The Dec plan was to hike once more and by 25 bps at the 'main' meeting in March. The bank will not signal that this plan is under reconsideration. Still, the bank will refer that growth has been slightly higher, and the labour market is somewhat tighter than assumed in Dec, and that core inflation was a tad higher too. The overall inflation outlook has become better though, due to the collapse in European gas and electricity prices
  - The **trade surplus** will probably decline further in December, as both oil and gas prices fell slightly. In January, the surplus will collapse, at the gas price may decline more than 50%
  - We expect at stabilisation in **SSB's manufacturing survey** – and a decline in **housing starts**

Sources: Bloomberg. SB1M est. in brackets. Key foreign & all Norwegian data are highlighted, **the most important in bold**

Global trade has probably slowed but retail sales, ind. production up in H2

*The upside in 2023: China, and the turnaround may already be underway, mobility has recovered already



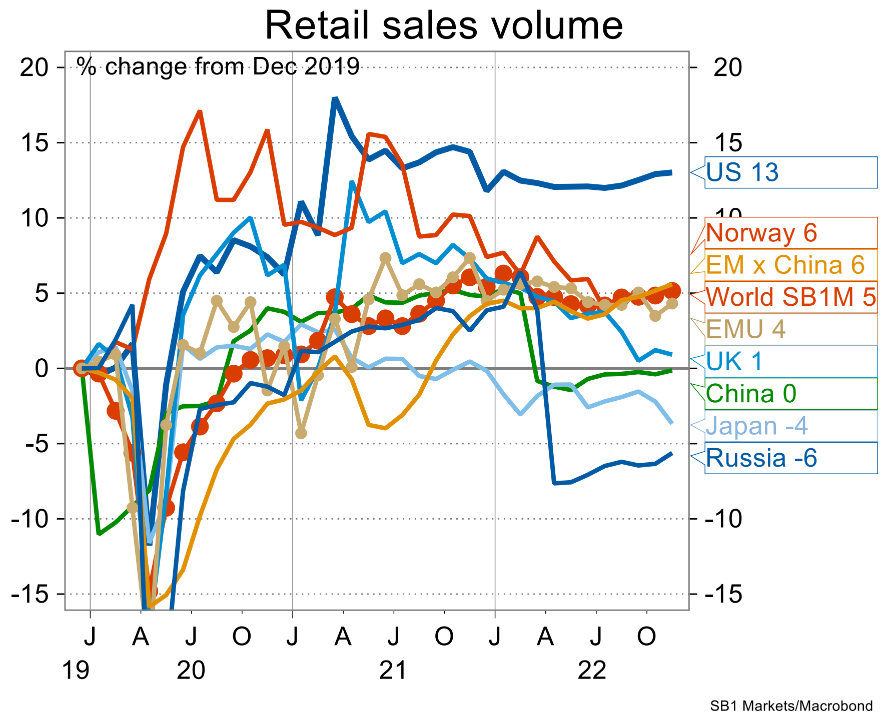


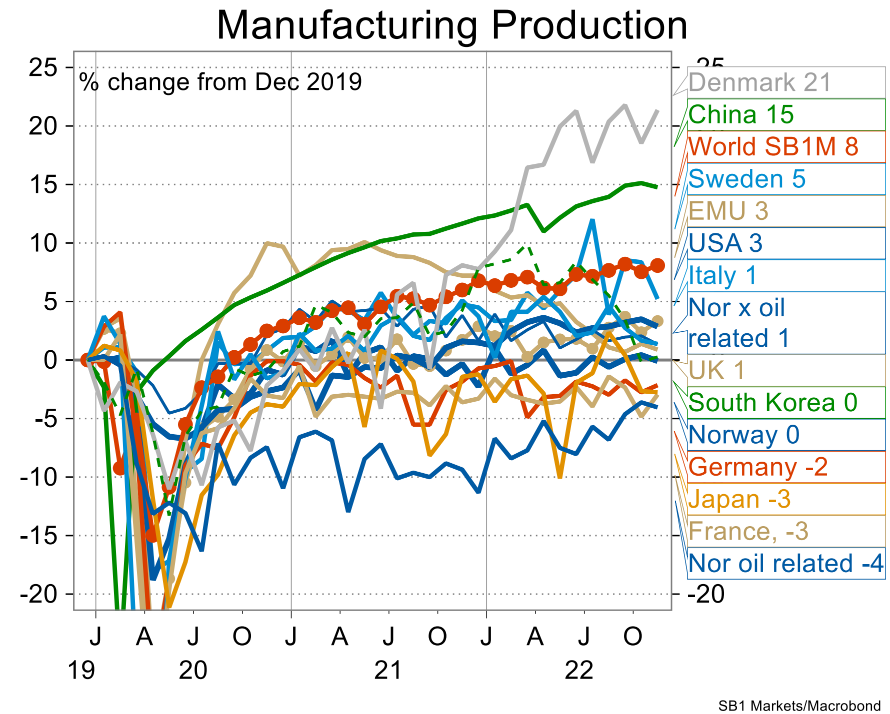
- Global trade was less weak at the end of last year than initially estimated by the Kiel institute - but trade is weak

Global foreign trade: The last months, including forecasts, are estimates from the Kiel Institute.

A broad slowdown of retail sales, at least in the rich part of the world (+China)

Manufacturing production is slowing too – and surveys signal a downturn

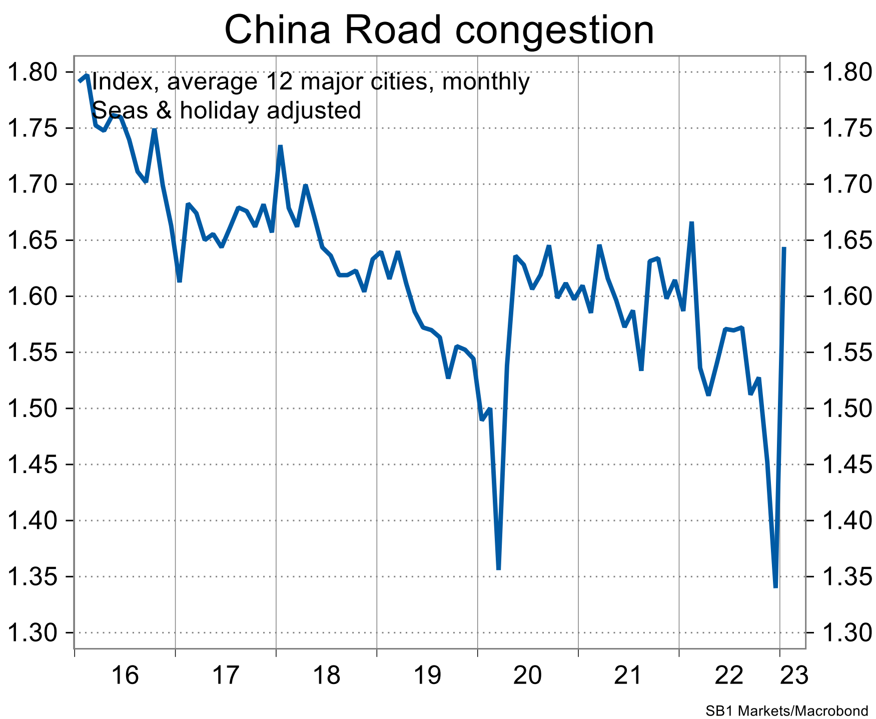


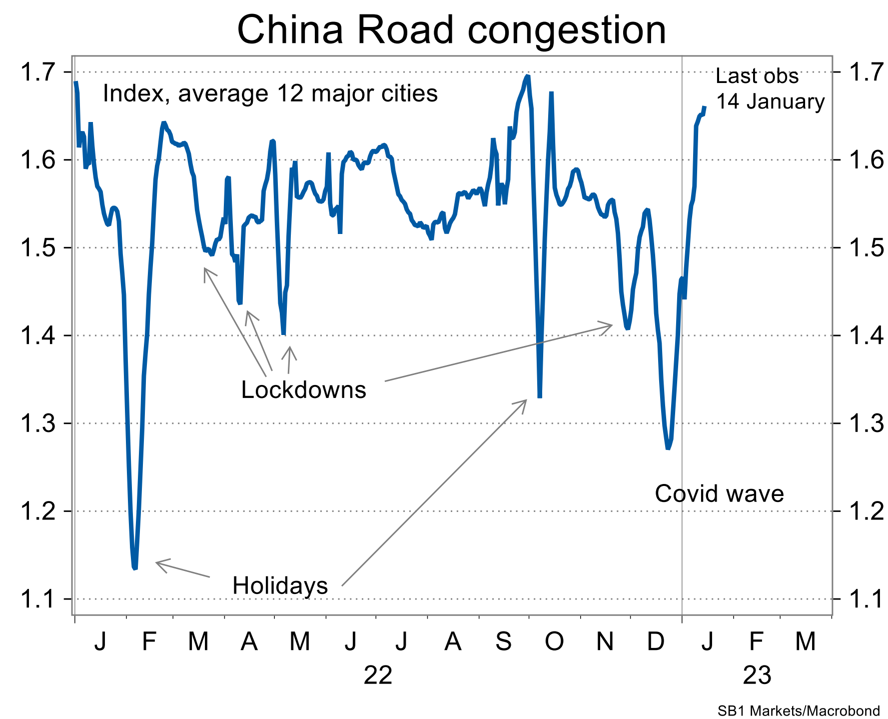


- Retail sales in China rose marginally in November but the history was once more revised down. The outlook is bright: Retail sales should pick up rapidly as soon as the current Covid wave of infections has burned through the population – and most of that may already be behind the Chinese, witnessing the sharp increase in mobility taking place now (check the two next pages)

US retail sales: Personal consumption of goods, ex auto & energy

Road traffic back to a normal level!



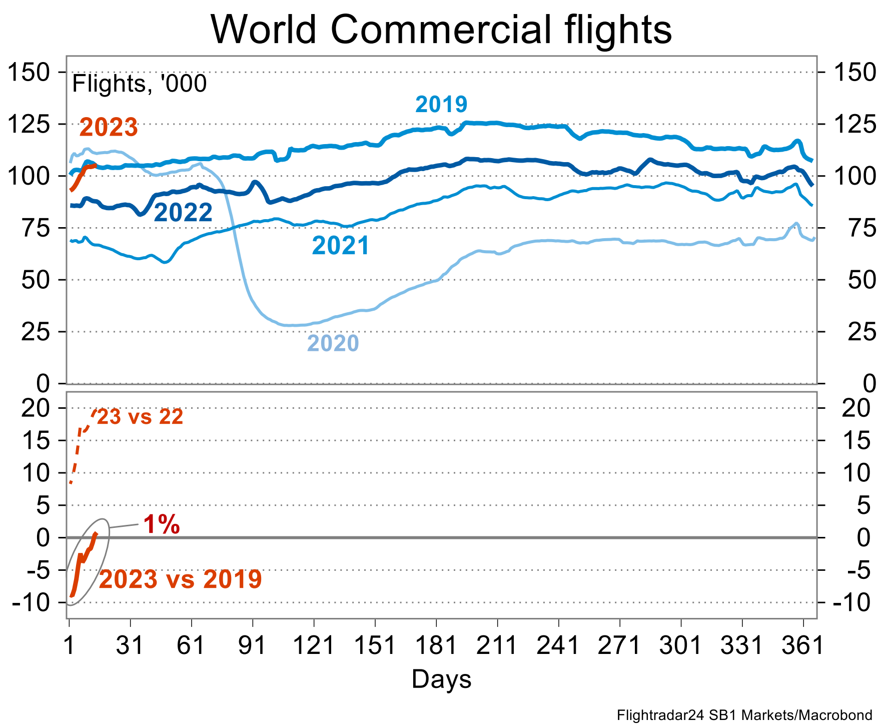


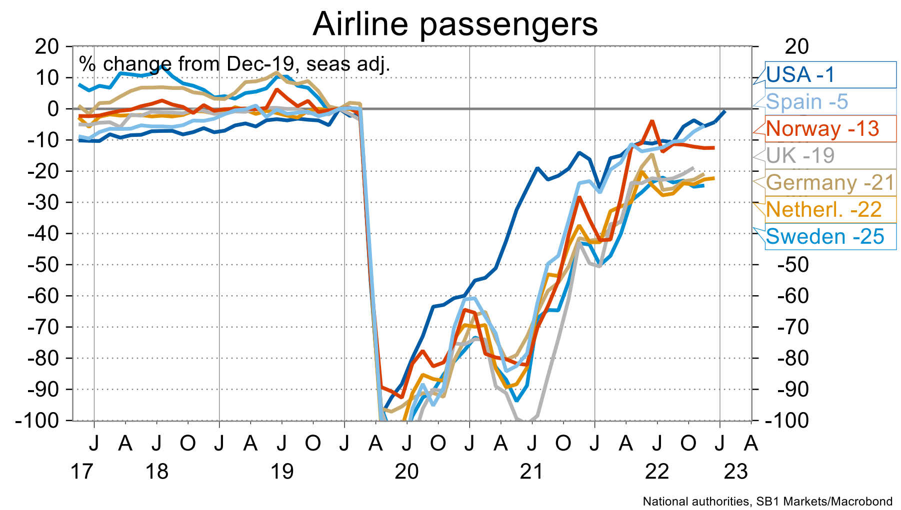
Metro traffic is rapidly recovering

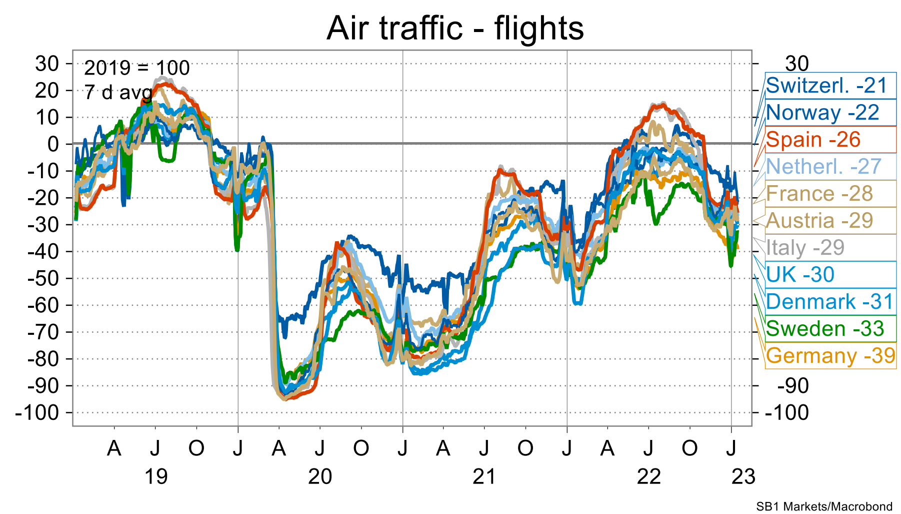
We are quite confident: before not too long, airline traffic will return (more or less) normal levels

A strong start for global airline traffic in 2023 – back up to the 2019 level!

Had growth rates been normal the past 3 years, it should have been at least 12% above



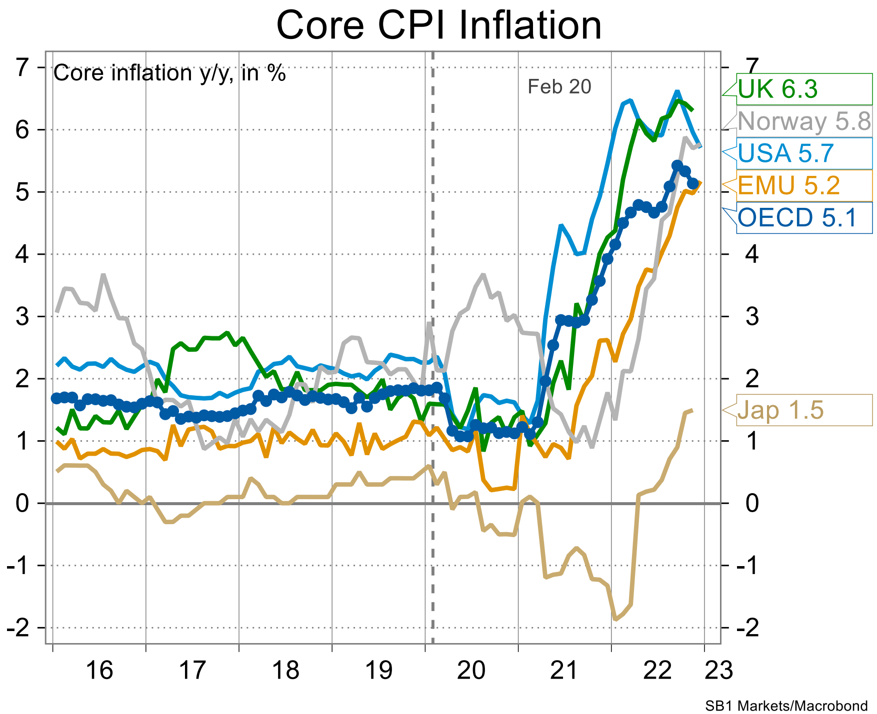


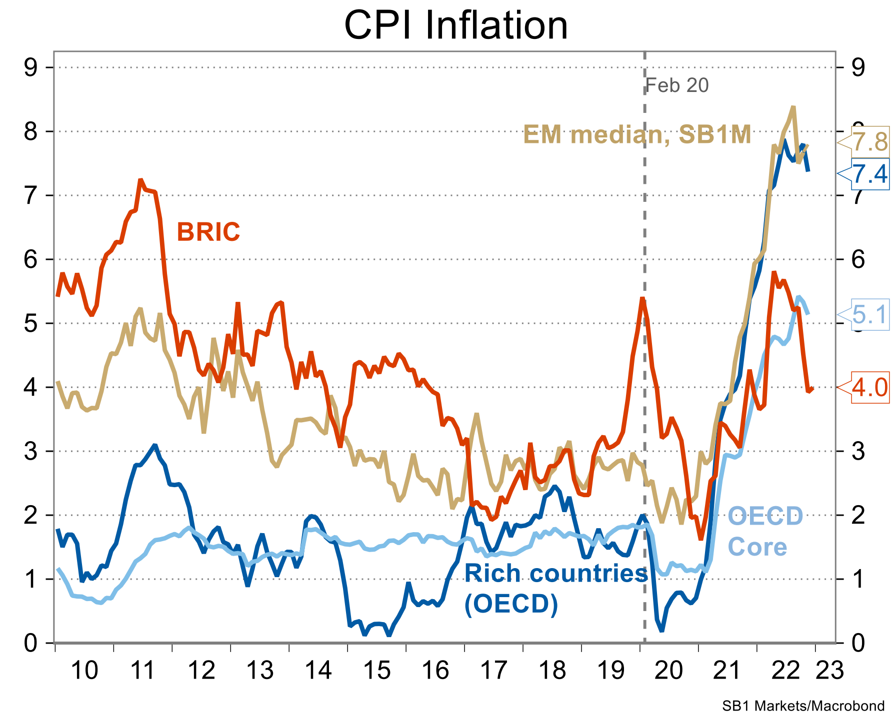


- Chinese traffic will now doubt come rapidly back (and that may already be happening)

Peak inflation? Very likely, both in developed & emerging markets

The going rate in DM is still 7% - 11% headline inflation, and 5% - 6% core inflation

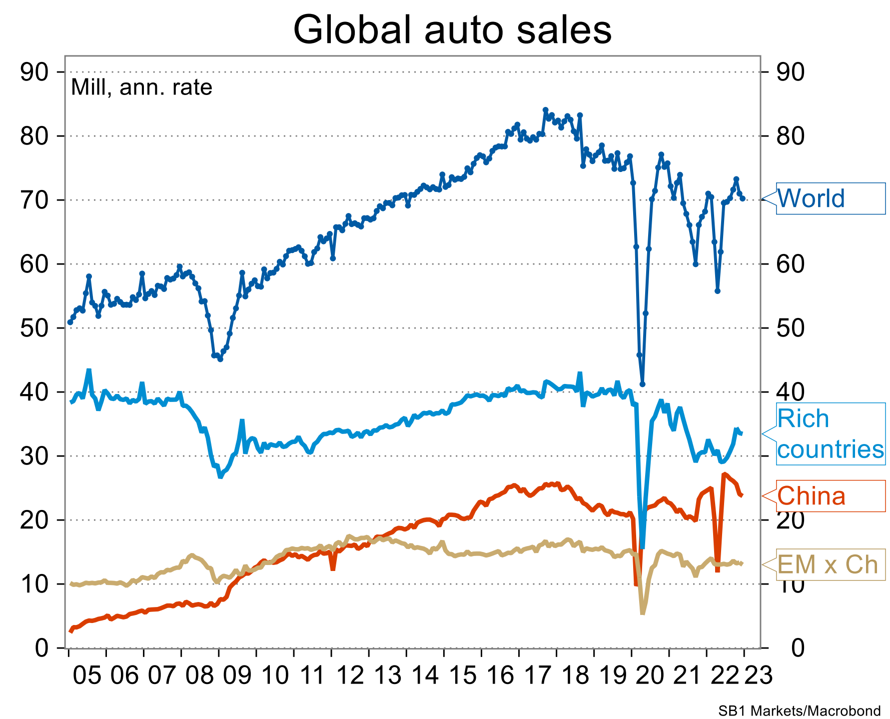


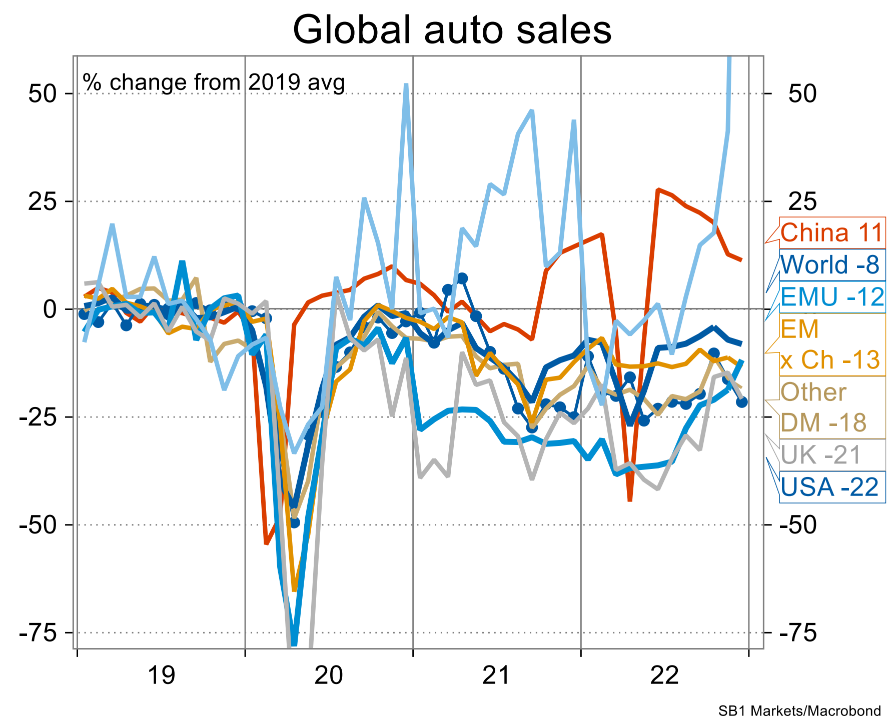


- We expect **inflation** to decline rapidly through 2023, as raw material prices and freight rates are declining, profit margins will come under pressure as demand, at least for goods, weakens in the rich part of the world. In the US, core goods prices are already declining (check next page)
- In Europe, the big uncertainty is of course **energy prices**. We still think the potential on the downside is larger than the risk to the upside, even if 2023 prices have fallen sharply recent weeks. Both demand and supply is adjusting to high prices – and prices will come down
- US has a wage cost challenge, EMU most likely has not – at least not until now. In the US wage inflation will slow the coming quarters as demand for labour weakens (the Fed will take care of that). The risk in Europe: Compensation claims in wage negotiations

Global auto sales further down in December, just EMU (and Norway) up

Sales declined in US and China – as well as in the average of EM x China, due to a decline in India

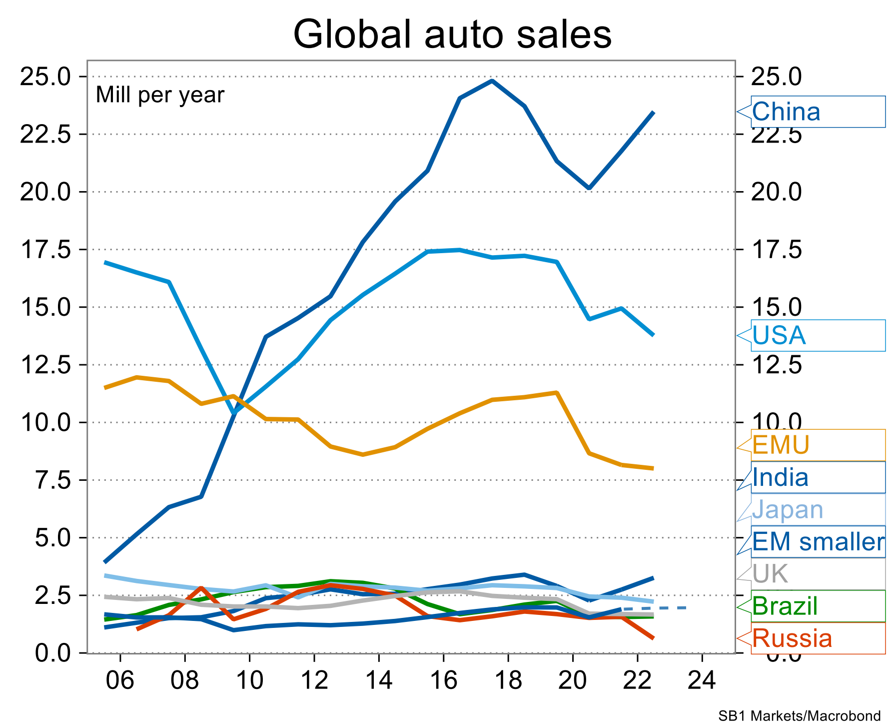


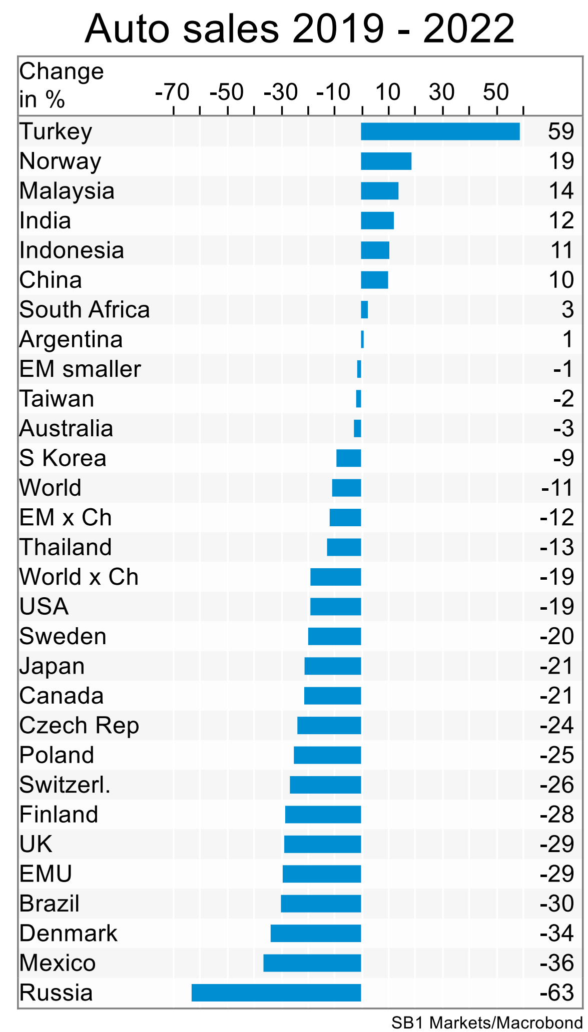


- **Global auto sales** fell 1% in Dec. Sales have been rather stable recent through H2, and are 8% below the 2019 level. However, 2019 is an easy comparison: Sales are down almost 15% from the peak in 2018 and 30% below the pre-2018 trend growth path!
- Sales in **China** fell further, but are still 11% above the 2019 level, even if housing is struggling (sales are still lower than in 2017). Sales in the **US** fell m/m and are down 22% since 2019. **EMU** sales continued upwards, primarily due to a surge in German sales, and EMU sales are 12% below the 2019 level. **UK** sales declined, and are down 21% from 2019! **Norwegian** sales were record high
- Sales in **EM x China** fell marginally, due to lower sales in India (but the level is high). Russian sales remain depressed
- **Auto production** has been the limiting factor, at last since late 2020. Now, the market balance is clearly better, and in the UIS we suspect demand to slow as well. Production has increased most places, and is higher than in 2019 some places.
  The US is just marginally below

China the winner in 2022 – and the largest market, by far

However, Turkey and Norway (!) saw the largest increase from before the pandemic!

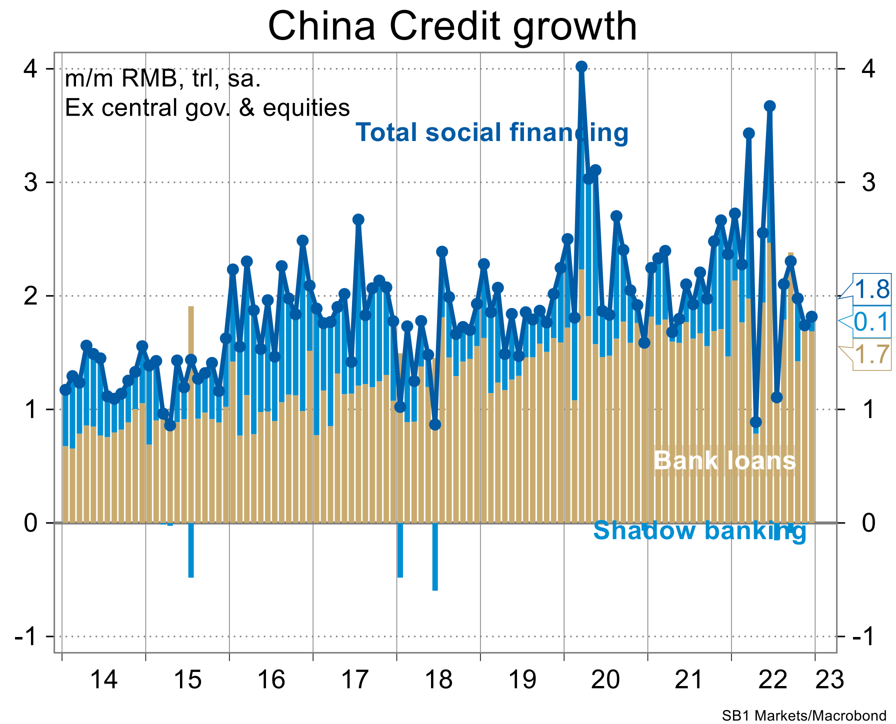


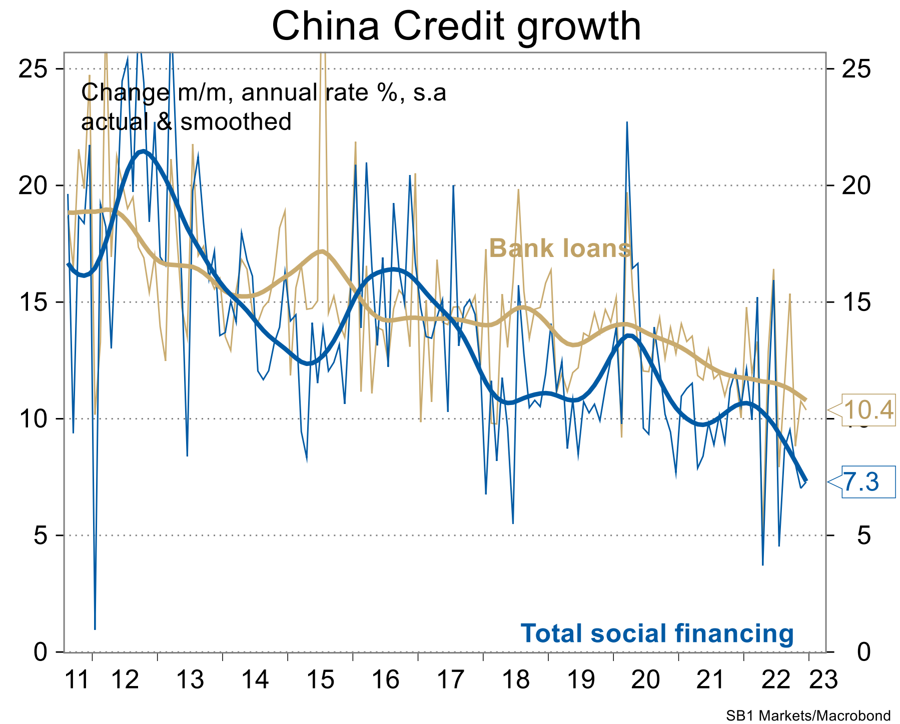


- **Global auto sales** were unchanged in 2022 vs. 2021. China contributed on the upside, US and Russian most on the downside
- From 2019:
  - **China** is up by 10% - but remain below the 2018 level.
  - **Indian** sales are up 12%. Russia is down 63%, at the bottom of the list
  - Most rich countries are down, by 19% in the **US**, 21% in **Japan**, while **EMU** and **UK** is down 29%
  - **Sweden** is down 20%, **Denmark** 34% - and **Norway** is up 19%

Slow credit growth in December too, and the trend is down

Covid, or a real ‘crunch’? We will soon find out ☺



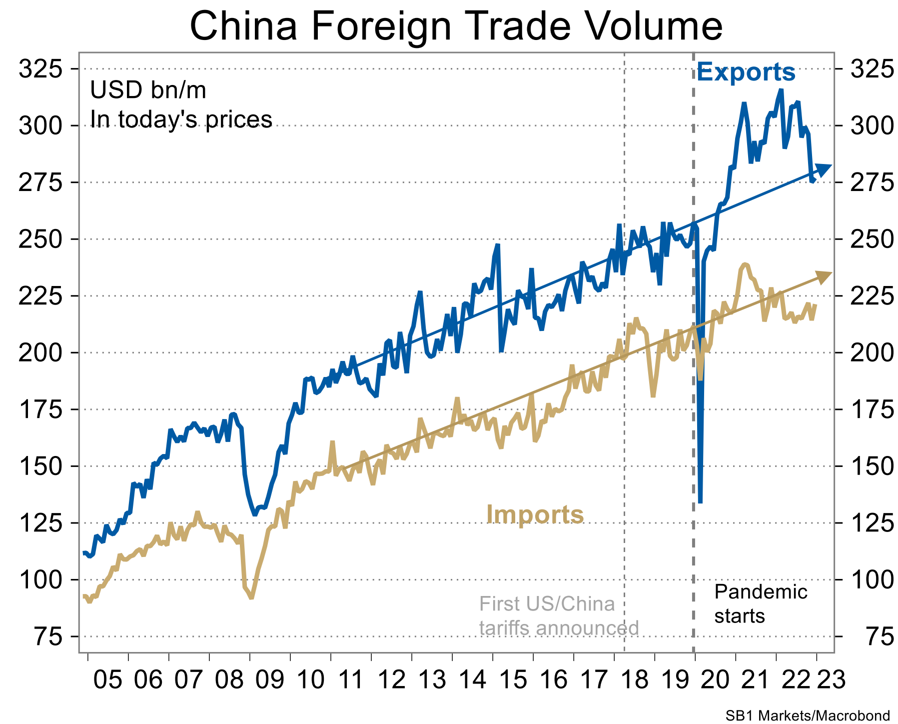


- **Core total credit** (social financing, ex central gov bonds, equites) grew at a 7.3% pace in Dec (m/m, seas. adj. annualised), up from % 7.0% in Nov (we initially assumed 7.7%). The trend is steeply down. The annual growth rate fell 0.3 pp to 9.5%
- **The official total social financing** rose RMB 1.0 trl, expected 1.6 trl. Our core credit supply grew RBM 1.8 bn (s.a.), marginally up from Nov
  - **Bank loans** rose by RMB 1.7 trl (s.a) or at a 10.4% annualised pace, well <u>above</u> expectations (actual 1.4 trl vs. exp 1.2 trl) . Loans are up 11.6% y/y
  - **Shadow banking credit** (all sort of credit outside banks) rose by just RMB 0.1 trl, and is up 5.3% y/y – but just 0.7% excluding local gov. bonds
  - **Local governments have been** responsible for most of the increase in credit outside banks over the last year , but growth has slowed recent months (including our Dec est., no data published yet)
- **Authorities** have announced several measures in order to stimulate the economy (and signalled that more will come), some directed towards the credit market, mostly to support the struggling construction sector

SpareBank 1 MARKETS

Exports flattened in Dec. Soon we'll get the 'first' real test on foreign demand?

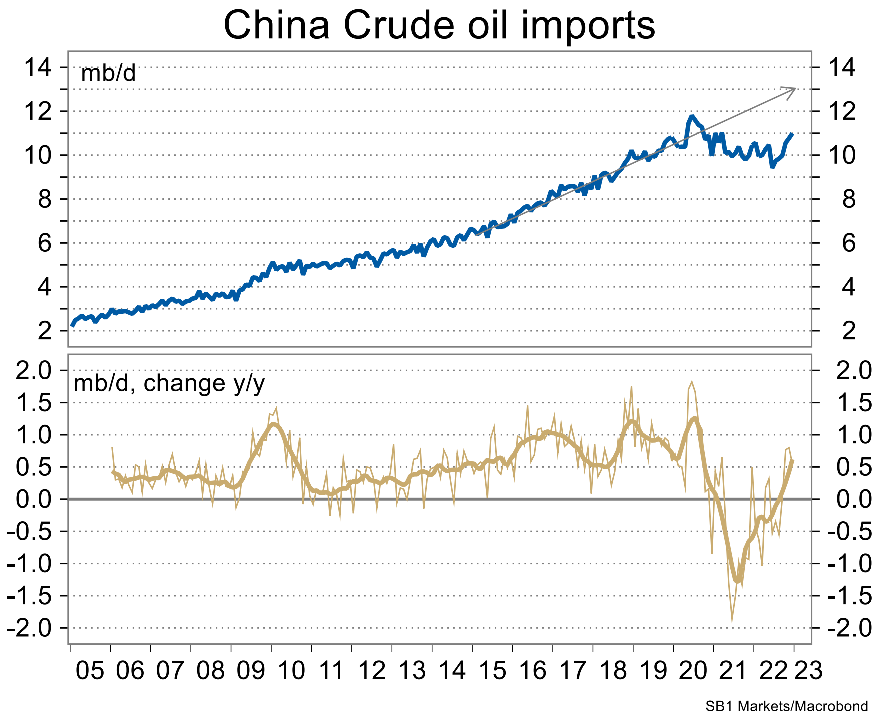
Exports fell sharply in November, probably mostly due to Covid restrictions/lockdowns.

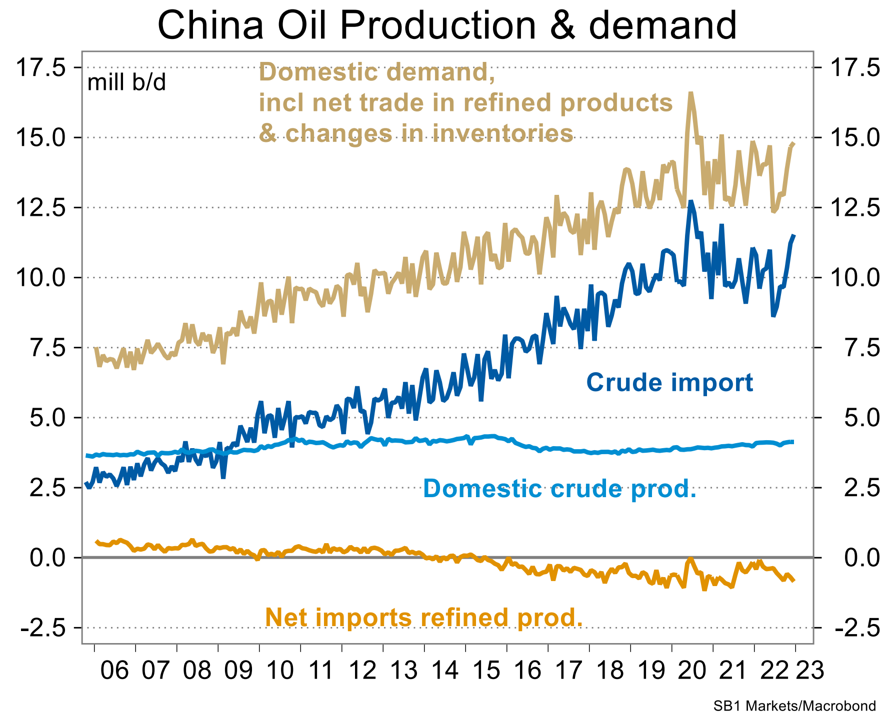


- **Export values were unch. in December** (in USD terms), following the 6% drop in November, to the lowest level since August 2021. Exports are down 10% y/y, 2 pp above expectations. Export values are still up 35% from before the pandemic, and **export volumes** are up 11%, and still not below the pre-pandemic trend (so much for the 'lack of supplies from China story', Chinese exports have been super strong through the pandemic. Exports were no doubt hampered, first by covid restrictions, and from the middle of the month the huge Covid wave and the sharp reduction in mobility. In January, mobility has shot up – and we expect exports for follow suit. However, demand from abroad has also weakened. Trade patterns may turn away from China but the impact will just be very gradual
- **Imports** rose 2% m/m, and are down 7% y/y, 3 pp above expectations. In value terms, imports are heading downwards, but recently not in volume terms. Still, in **volume terms** imports are down by 7% from the peak level last spring – and some 3% below the pre-pandemic trend path (which is not a disaster)
- The **trade surplus** at USD 79 bn, as expected, but 'just' 56 bn seasonally adjusted, and is now trending down

Crude oil imports up 1 mb/d recent months, 2 more to go?

China will ‘reopen’ as the Covid wave most likely is on the retreat. Transport activity has recovered. More oil needed?

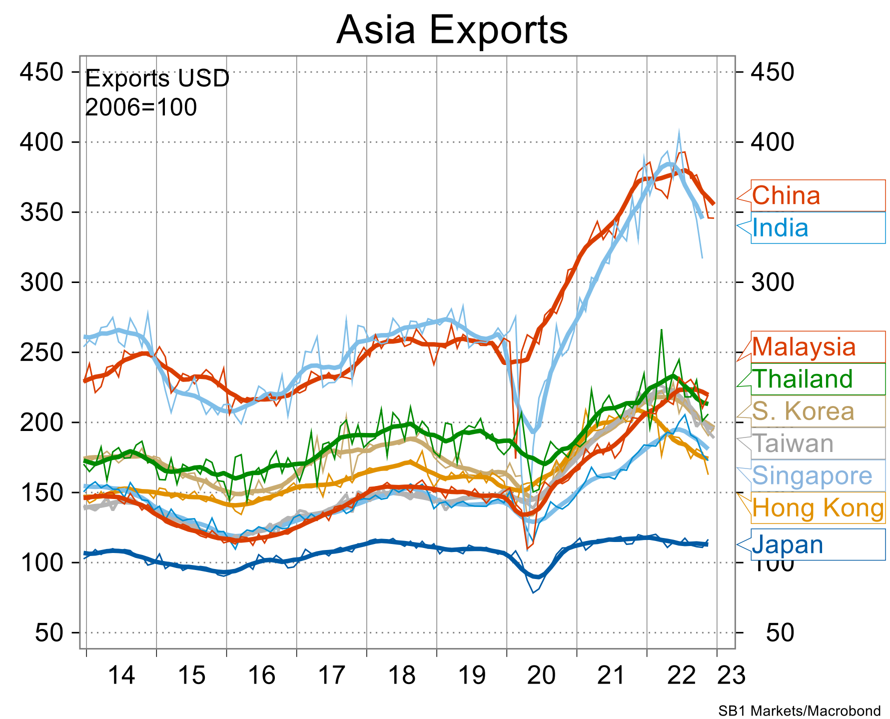


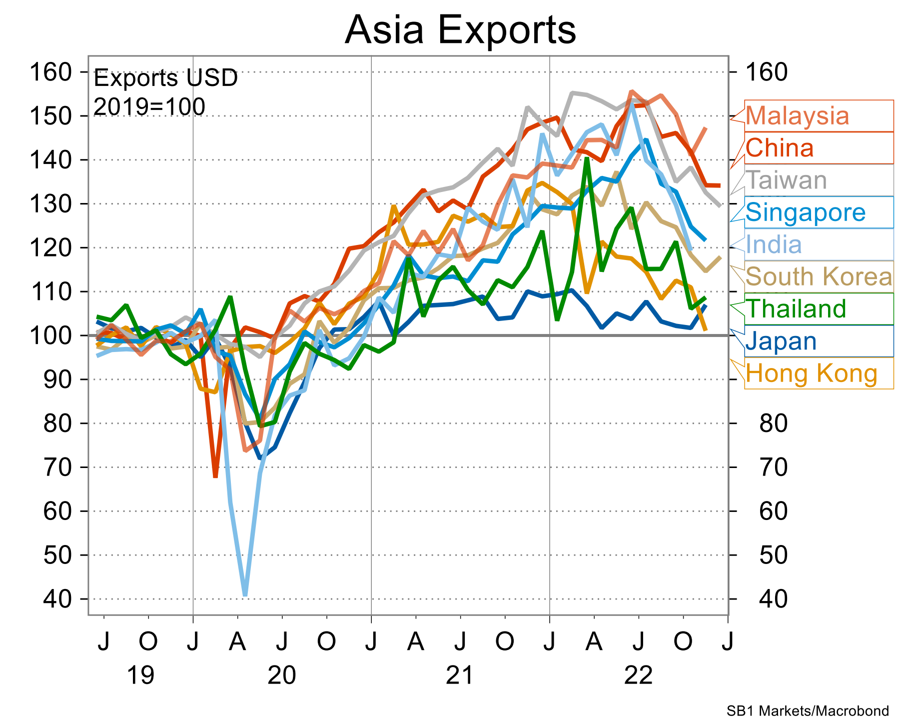


- The pandemic has reduced **road transport** (both persons & probably also goods). In addition, **construction activity** has fallen from early 2021
- **Demand for oil** will very likely increase as the society and the economy is now returning to more normal ways of life. **Road traffic** has recovered rapidly recent weeks/day, and airline traffic will very likely follow suit. However, construction activity may harder to get back to normal, keeping diesel demand lower than normal for still a while

Exports from all other Asian countries on the weak side recent months

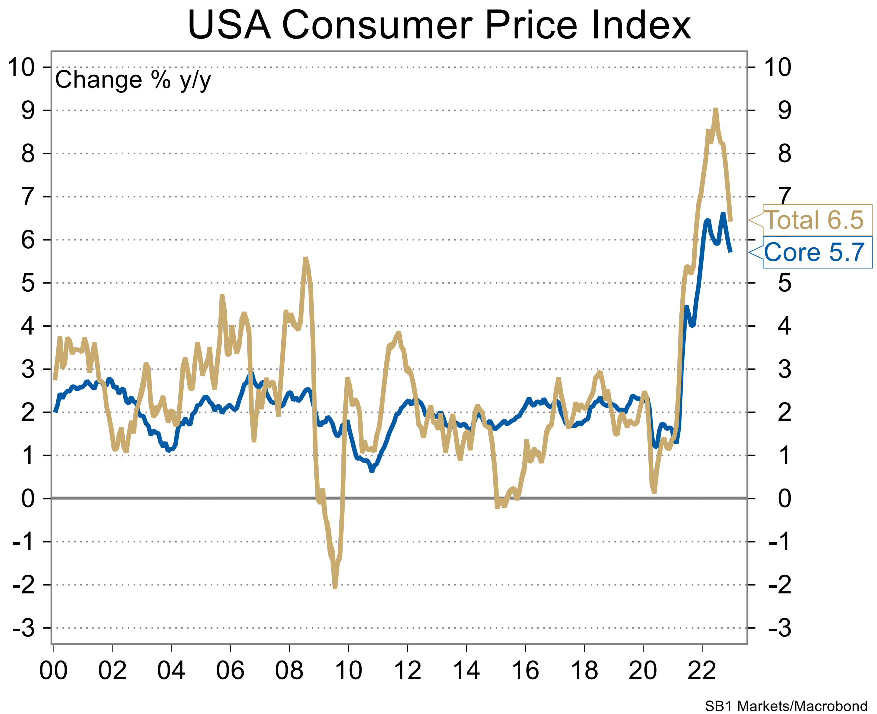
… which confirms the lack of global demand story – not a sudden production problem in Asia

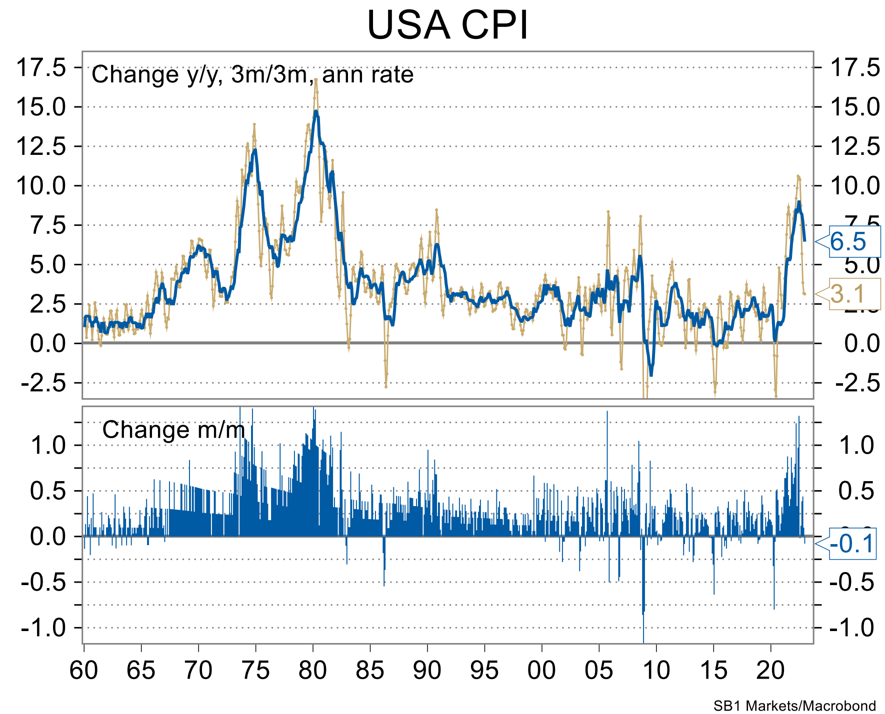




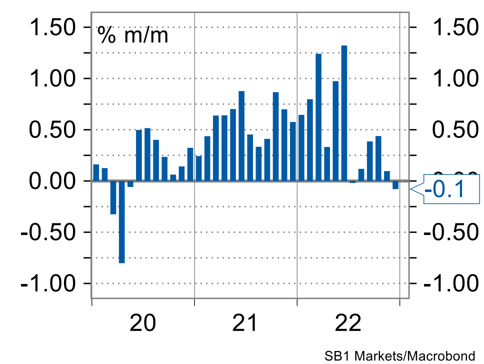
CPI has peaked. More to come

CPI fell 0.1%, as expected and the annual rate fell to 6.5% from 7.1%



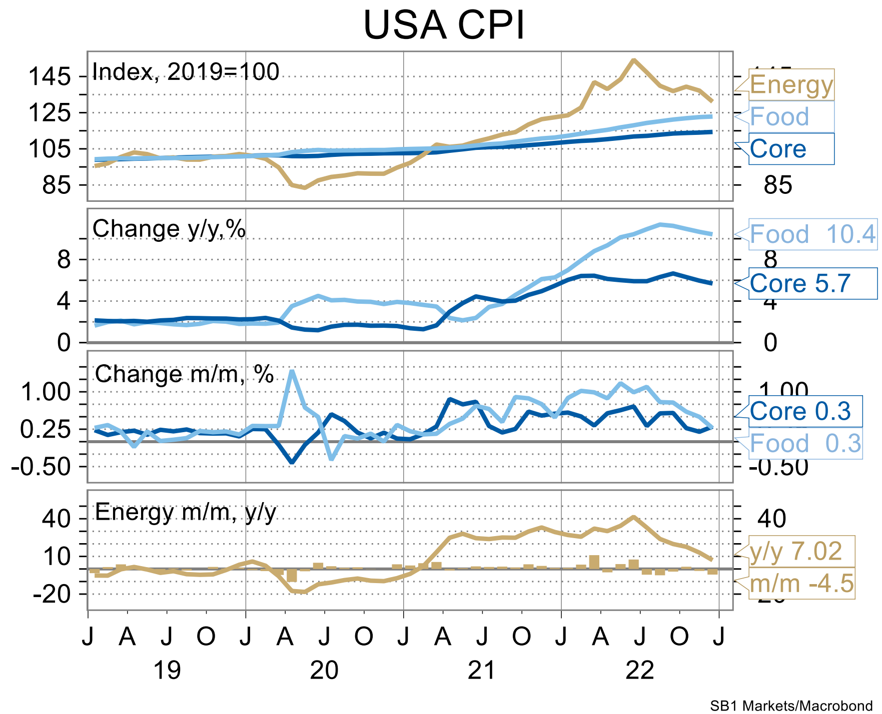


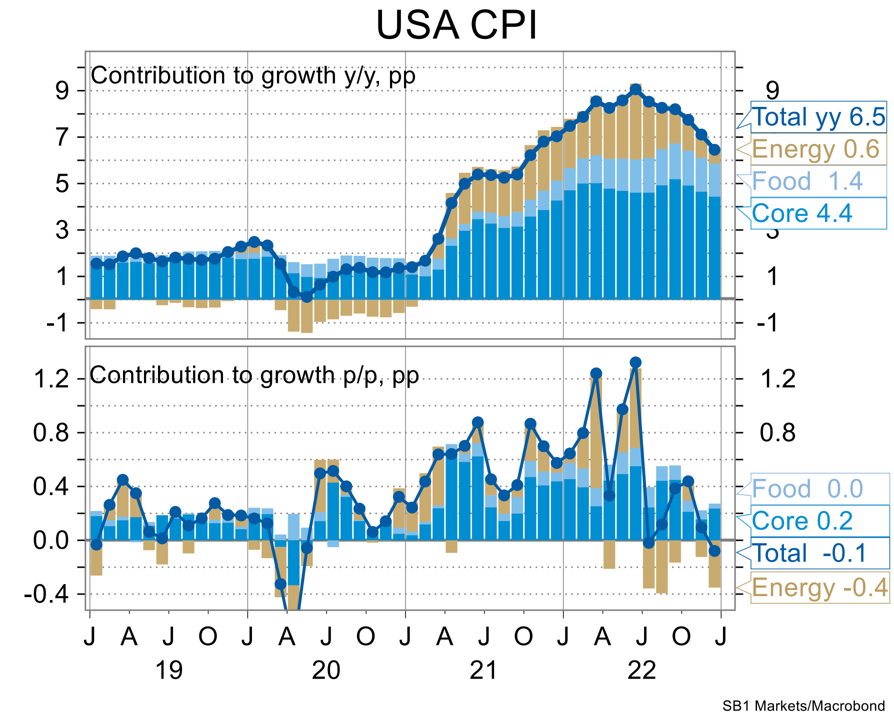
- **Headline CPI** fell 0.1%, the first monthly decline since spring 2020, when prices fell sharply. The annual rate slowed 0.6 pp to 6.5% in December, as expected, the 6th monthly decline in row. The 3m/3m rate fell to 3.1% - from above 10% some few months ago
- **Surveys** report a rapid slowdown in price increases, especially ISM markets, and the NFIB survey (check here)
- **Markets** rallied, for good reasons. Inflation is definitely on the way down. Now, the decline in driven by lower corporate margins, and that's just a temporary relief. Wage inflation remains Fed's main concern, but even here news have been on the positive side recently, and last week the Atlanta Fed median wage tracker slowed somewhat – but all wage indicators still report wage inflation well above a level that will yield 2% CPI inflation



Energy prices are falling, food price inflation is slowing – as is core inflation

Energy prices will soon turn negative y/y. Food prices are much higher than food commodity prices suggest

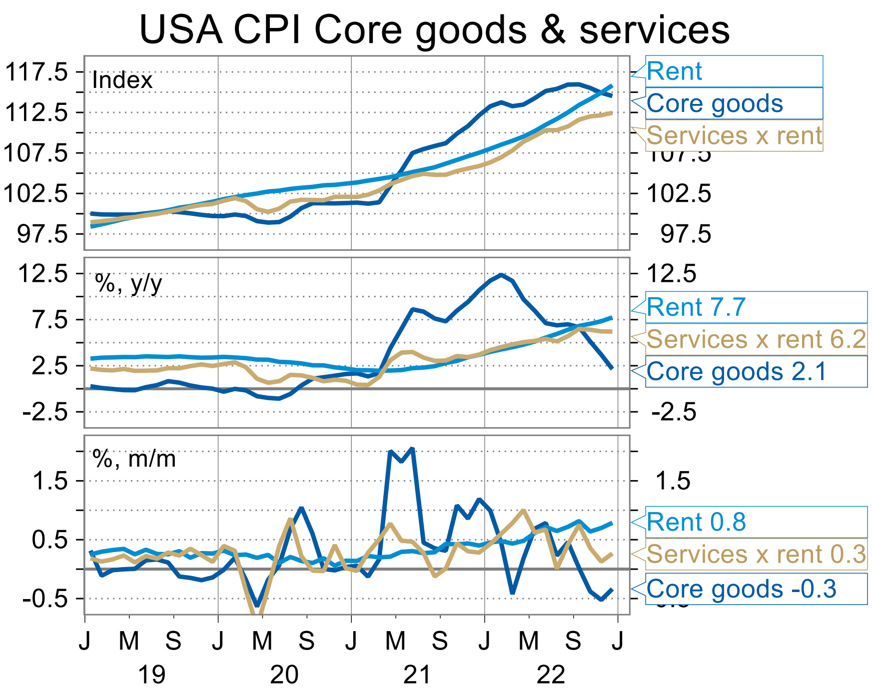


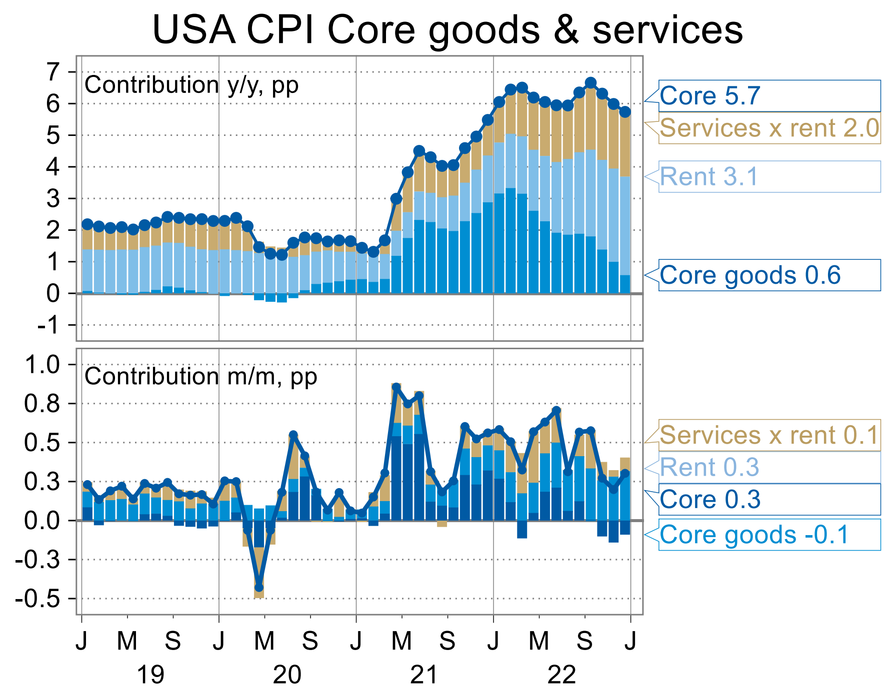


- **The headline CPI** fell 0.1% in December, as expected. The annual rate fell to 6.5% from 7.1%, also as expected. The trend is down both for monthly and annual growth rates
- **Energy** prices fell 4.5% m/m, and will very likely decline further in January. Prices are still up 7% y/y, contributing 0.6 pp to growth in annual headliner CPI
- **Food** price inflation is slowing but prices rose another 0.3% in December – but monthly growth is slowing rapidly. Prices are up 10.4% y/y, contributing 1.4%
- **Core inflation** has clearly peaked too, as goods prices are now declining (more next page)

Core goods prices are falling – services inflation slowing. But rents…

Core goods prices fell 0.3% m/m in December, and are up just 2.1% y/y, from 12.5% at the peak in early 2022



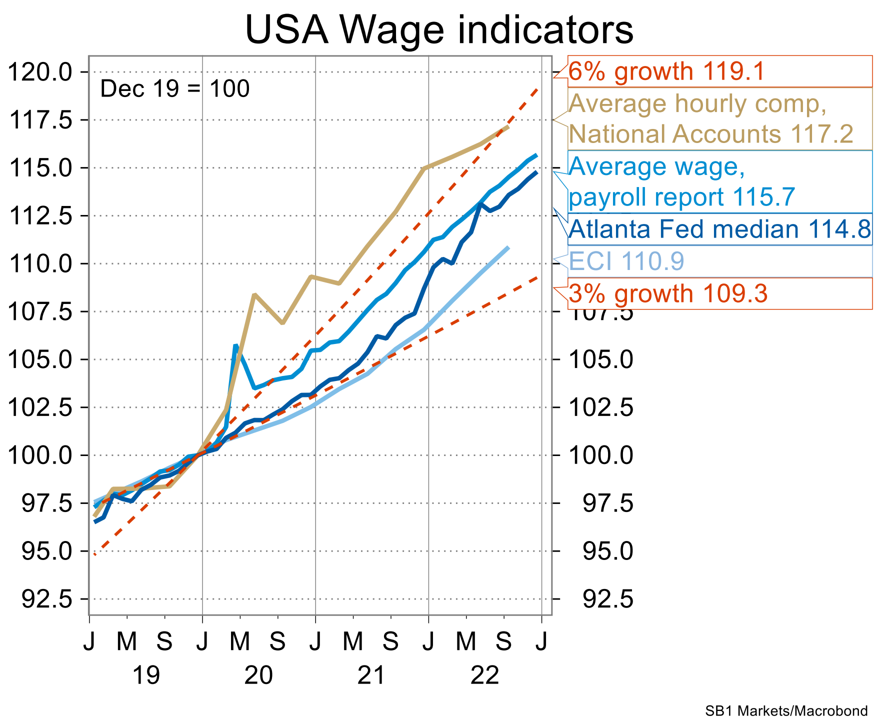


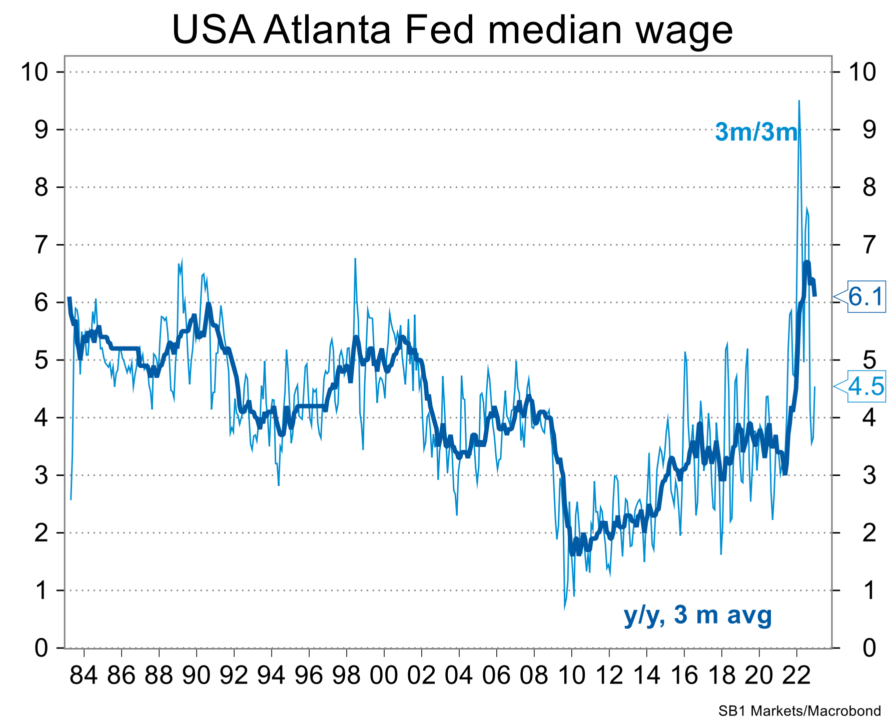
- A further normalisation of **goods prices** is likely, as demand slows, raw material prices are coming down, alongside transportation costs – and as signalled by the PPI
- **Rent inflation** is still on the way up – up 0.8% m/m and by 7.7% y/y! Rents on new leases very likely are moderating, the rent index in the CPI should follow suit after some months
- However, as Powell has stressed several times, also at last week's press conference, inflation will not come down to a sustainable level before **service sector inflation** (ex residential rents) also yields. Monthly changes have slowed somewhat recent months, and the annual rate has probably peaked, but remains at 6.2%, unchanged from November
- *More details on the following pages*

In the core CPI: Rent 40%,

Atlanta Fed's median wage tracker has also peaked

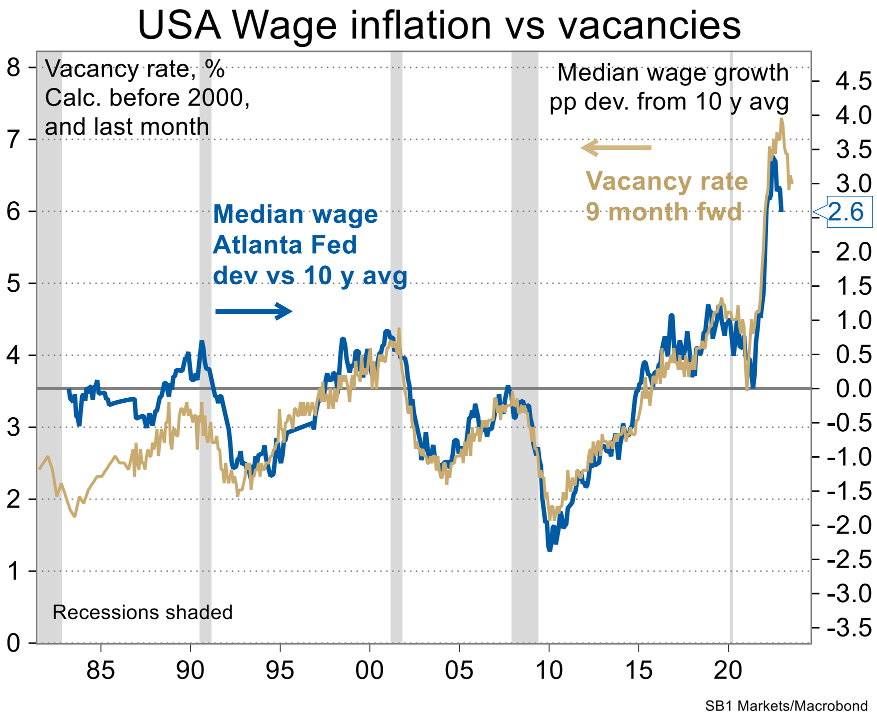
Even if the annual rate remains above 6%, underlying growth has slowed to below 5%. Still some 1.5+ pp too much





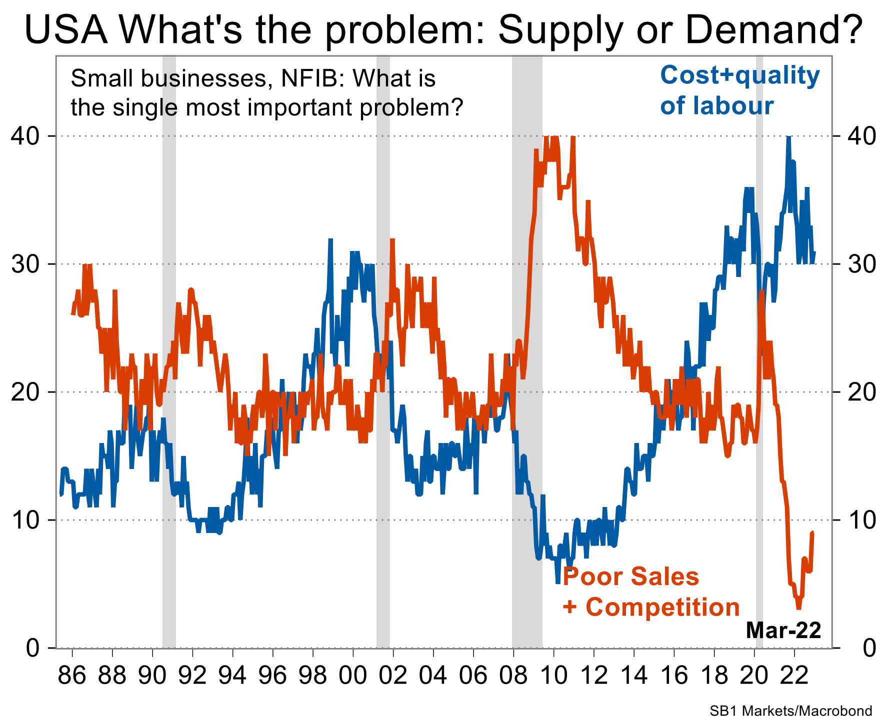
- **Wages** rose some 0.4% m/m in December (our calc.)
- The non-smoothed annual rate fell 1 pp to 5.5% (due to a rapid lift in wages in December last year), but even the 3m smoothed rate declined 0.3 pp to 6.1%. The peak was at 6.7% in June/July last year
- This series is somewhat volatile but the underlying trend has fallen to 4.5% – 5% recent months

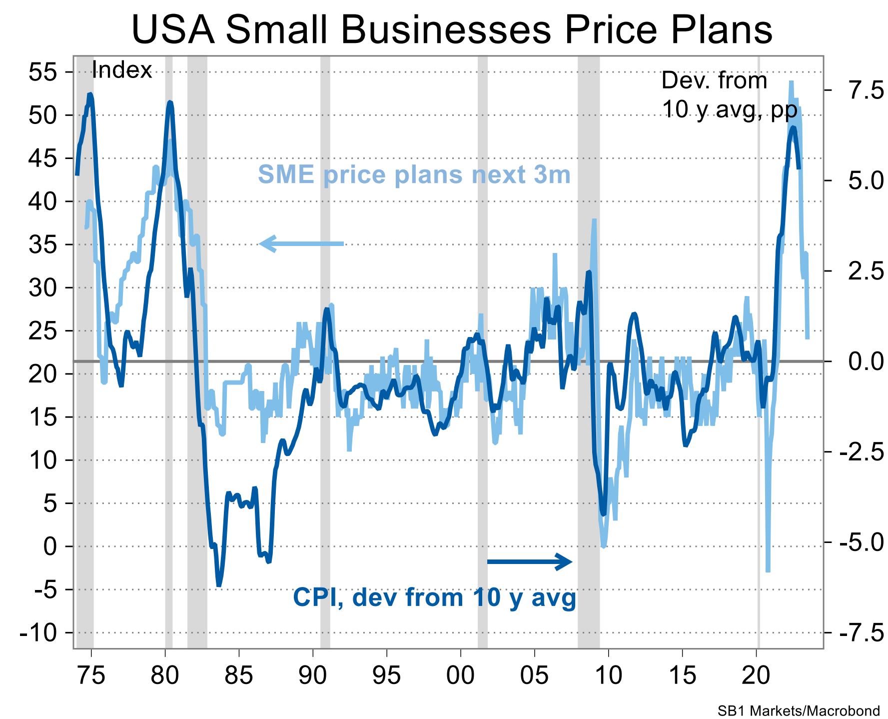
Wage inflation is slowing, but remains too high



Price increase plans are ‘collapsing’, the 3rd largest drop ever!

Even if sales/compensations are not yet the problem, lack of labour still is!

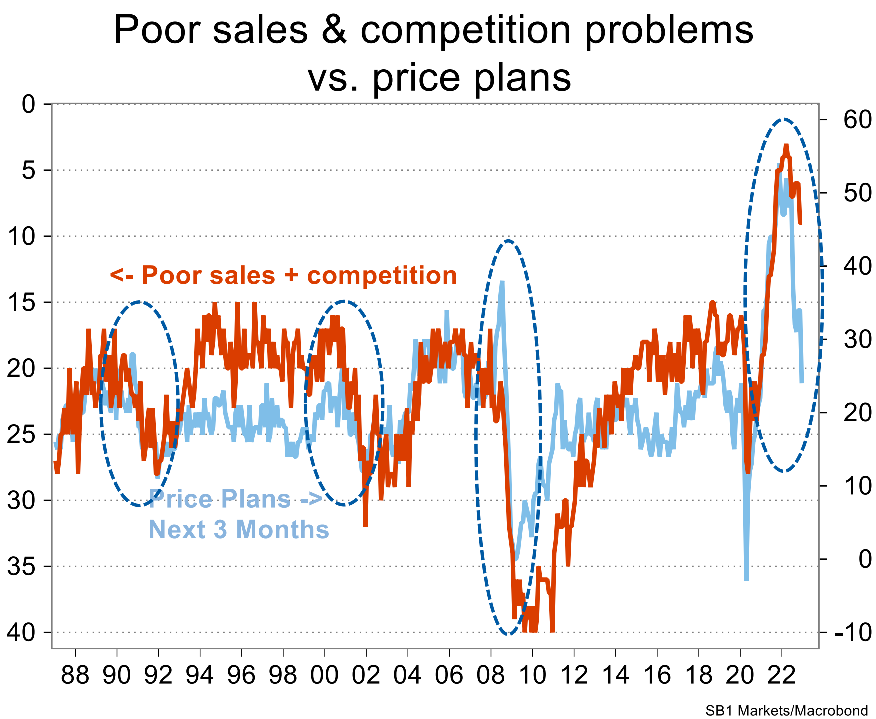




- **The ‘gap’ between supply and demand concerns** is still very large, but it is now heading down
- Very few companies report **poor sales** as a problem, somewhat more complain about **competition**. The total share is up from March, and increased further in Dec. **Cost & quality of labour** are stated as the most important problems for a much higher share of companies than normal. However, the share has fallen somewhat from the peak (but not further in December) – and compensation plans were revised up!
- The share of **companies that plan to lift prices** has fallen sharply from the peak and fell 10 pp to 24% in Dec, not far above the average at 21%! The decline was the 3rd largest ever! This is really encouraging new for the Fed! Price plans are coming down before sales have become weak! This is rather unusual, check next page
- We still expect the sales/competition to become the major worry for small businesses – but are less sure than before this report!

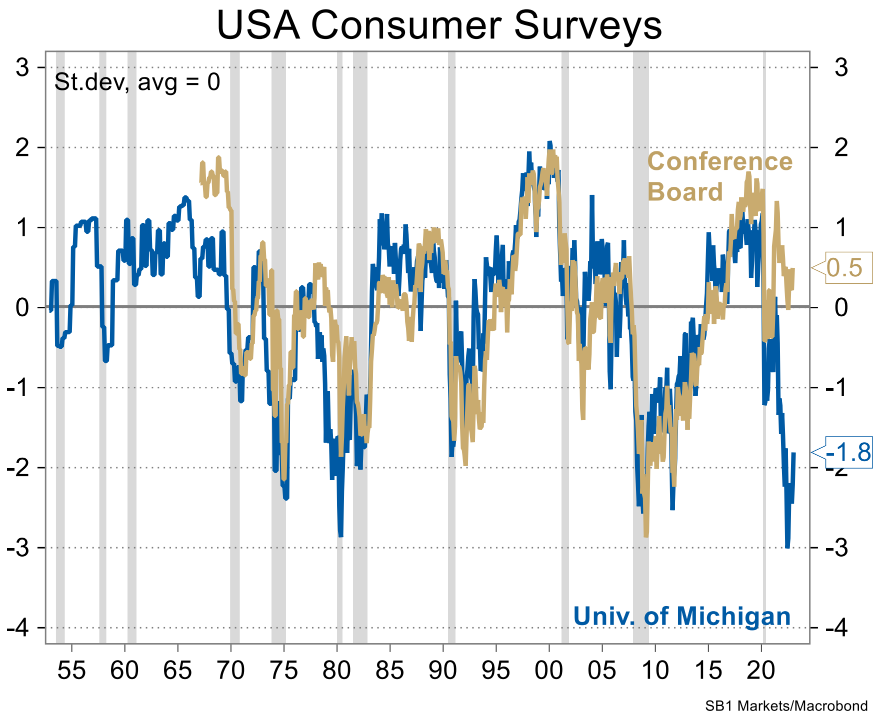
Prices plans have retreated, before poor sales has become a problem

… which is not the norm!



Univ. of Mich. sentiment further up in early January

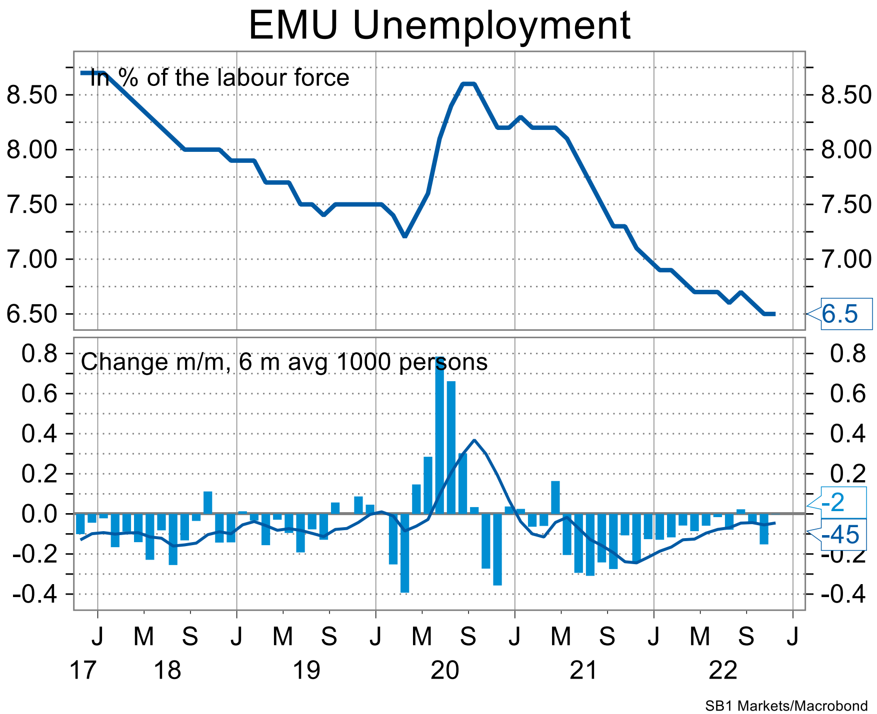
The sentiment index is still at a low level, 1.8 st.dev below average. All other surveys have turned up

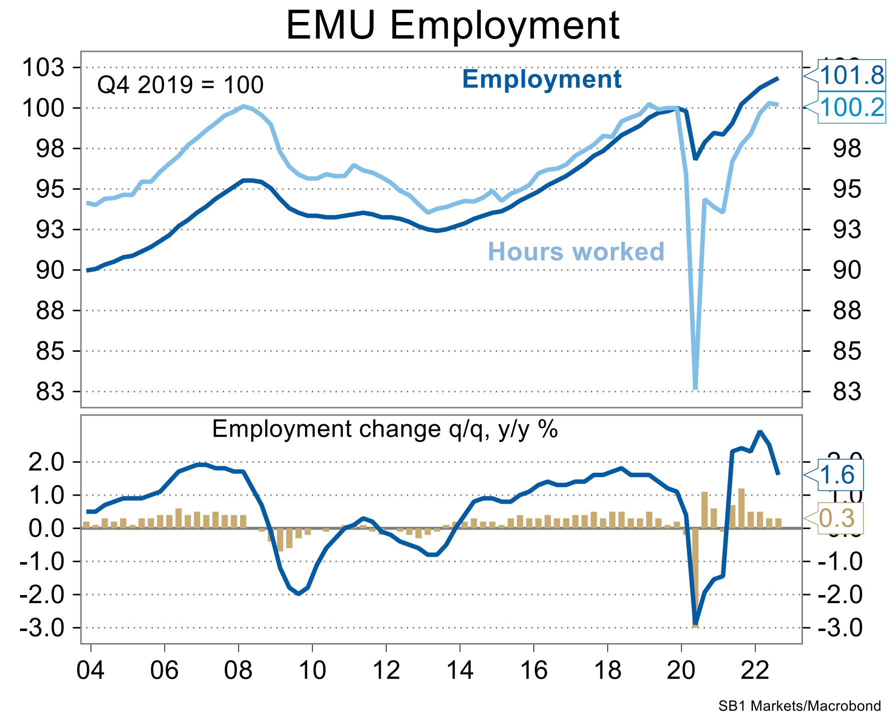


- **University of Michigan's consumer sentiment** climbed 4.9 p to 64.6 in the first part of January, expected 0.8 pp. The level equals 1.8 st.dev below average, after a 0.4 st.dev lift. The bottom was in in last June, at -3.0
  - Both households' assessment of the current situation and expectations fell in November, expectations the most
- **The 3 other consumer surveys** all turned up recent months
- **Short-term inflation expectations** fell significantly, for the coming 12 months to 4.0% from 4.4% in November, and from 5.4 at the peak. The 5y expectation rose 0.1 pp to 3.0%
- **The risk:** The UM survey is still at a very low level, and is often an early bird in the cycle

Unemployment stable at 6.5% in November, the lowest level since 1989

The no. of unemployed was unch. m/m, following a 45' drop last month. Employment is still growing

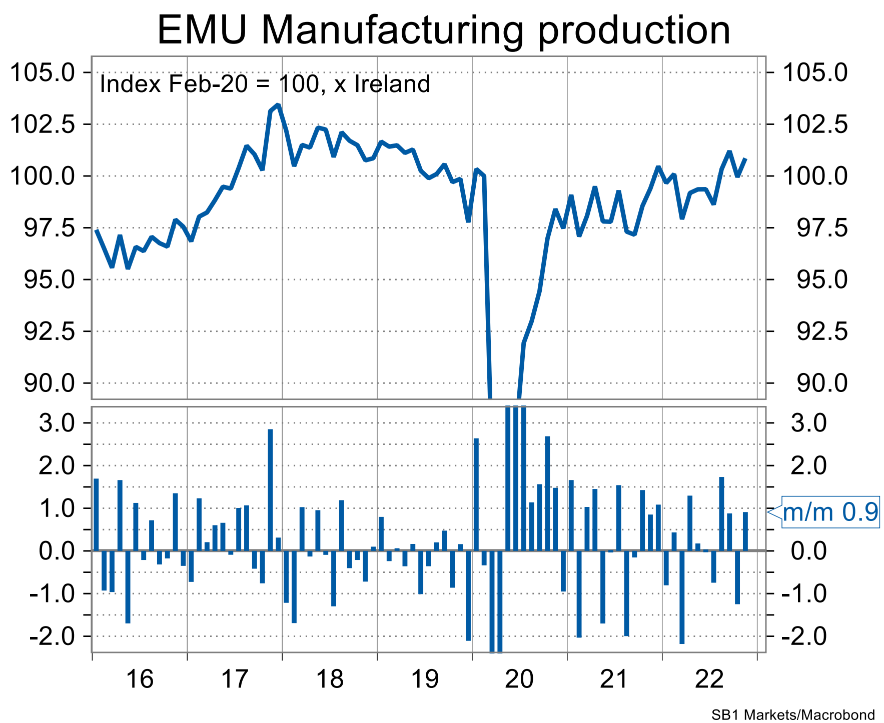


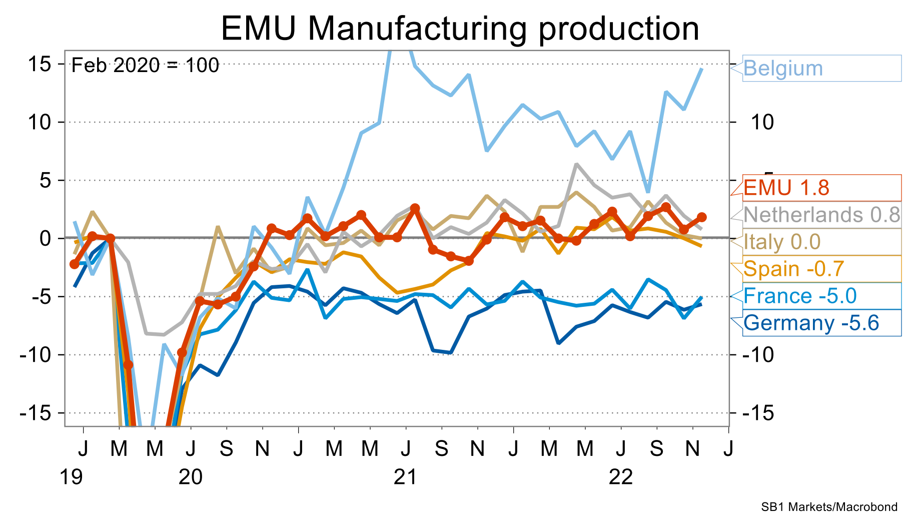


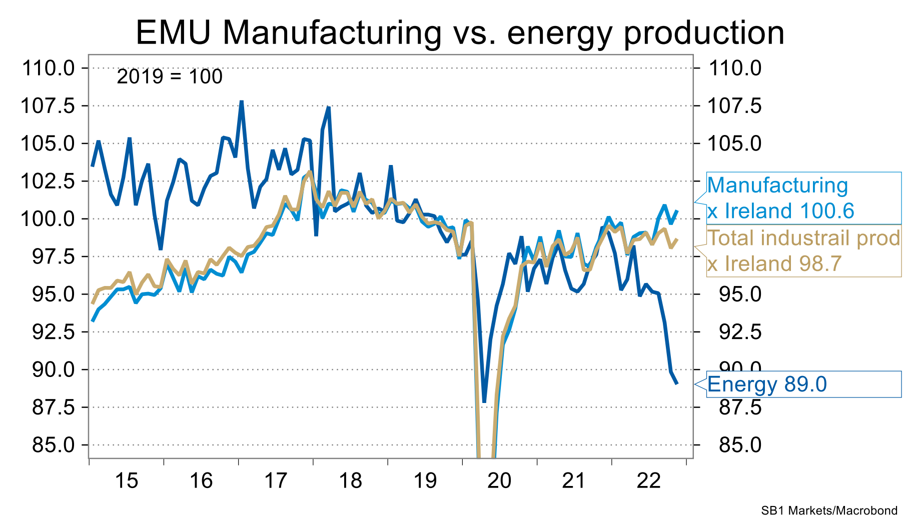
- **The unemployment rate** was unch. at 6.5%, as expected. The number of unemployed persons fell by 2'
- **Employment** grew by 0.3% in Q3 (not annualised). The employment level & the employment rate are both higher than before the pandemic
- The number of **unfilled vacancies** is still high, but seems to have peaked
- The labour market is no doubt still very tight – until further notice
- **Wage cost inflation** has not accelerated but a slowdown in productivity growth has pushed labour cost per produced unit upwards, to somewhat above 2%

EMU manufacturing production up 0.9% in November, and the trend is OK!

Energy production is falling (10% ‘too low’) but manufacturing is not that hard hit





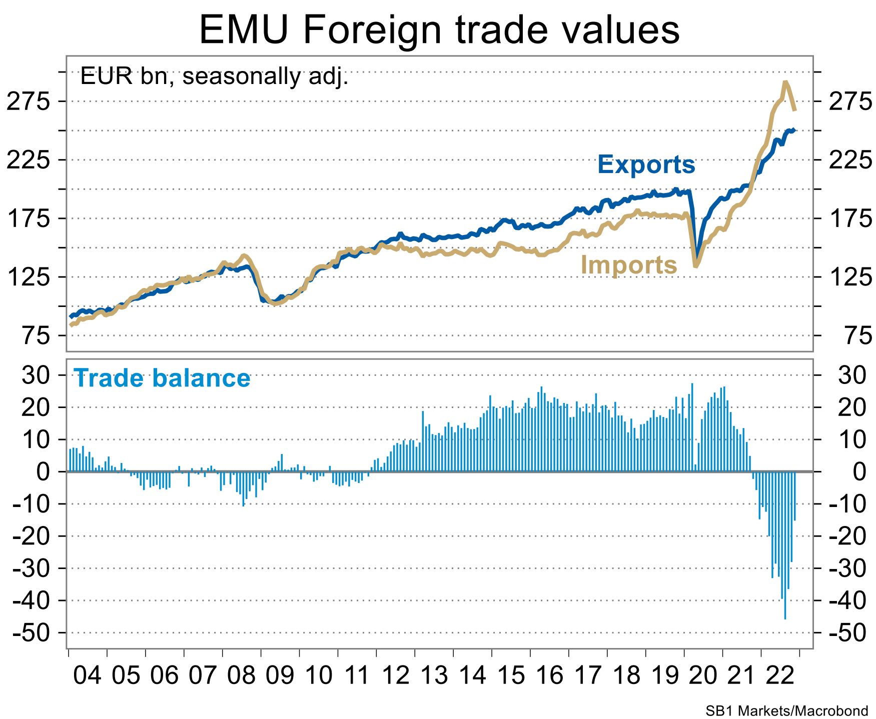


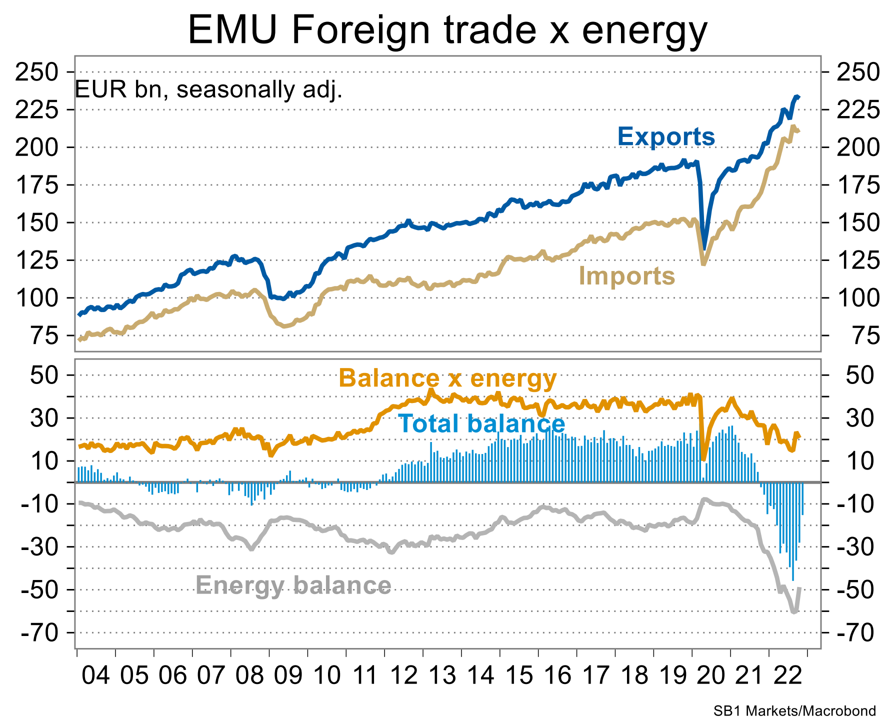
- **Overall industrial production** in EMU gained 1% in November, twice as much as expected. Ex (volatile) Ireland, production rose by 0.6%, which is a more relevant figure
- **Manufacturing production** x Ireland rose by 0.9%, and the short term trend is clearly up (3m/3m + 5.1%!), way better than we expected some few months ago. The energy crisis has not killed the manufacturing sector, at least not so far. Production rose most places
- **The short-term outlook:** Several surveys are weak – but they have stablised, and some surveys are still signalling growth

SpareBank 1 MARKETS

The trade deficit sharply down – due to cheaper energy imports

.. And a lower import volume. The overall deficit equals 1.4% of GDP, down from 4.1% in August!

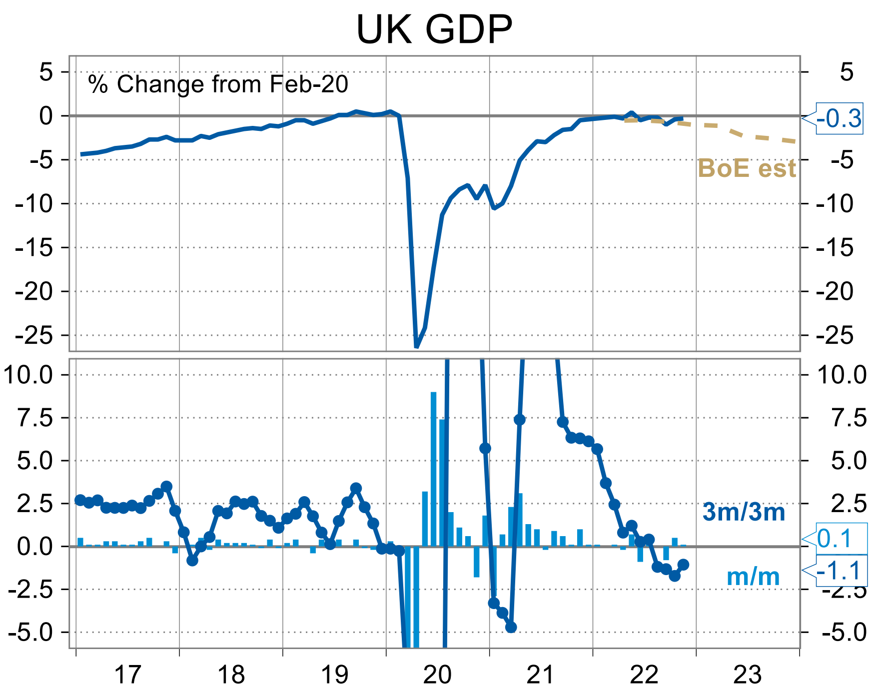


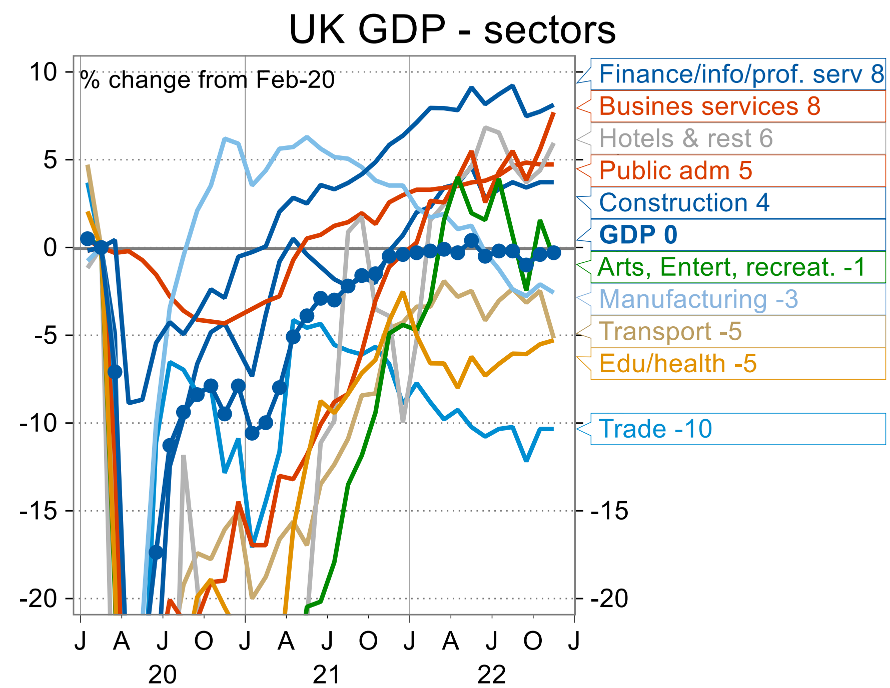


- The **trade deficit** narrowed in further in November as energy prices fell, to EUR 15 bn (s.a.) from EUR 28 bn in October. The trade deficit equalled 1.4% of GDP
- **Energy imports** fell and the energy deficit was reduced more than the overall , and the non-energy balance weakened slightly – but is at 1.8% of GDP, in plus
- **Imports a**re up 21% y/y, while exports are up just 17%. In volume terms, quite another story: exports are close to flat, while imports have soared (but fell in November), check next page

GDP surprised to the upside for the 2nd month – up 0.1% in November…

…expected <u>down</u> 0.3%. GDP has been trending slightly downwards from the spring, and is down 1.1% 3m/3m

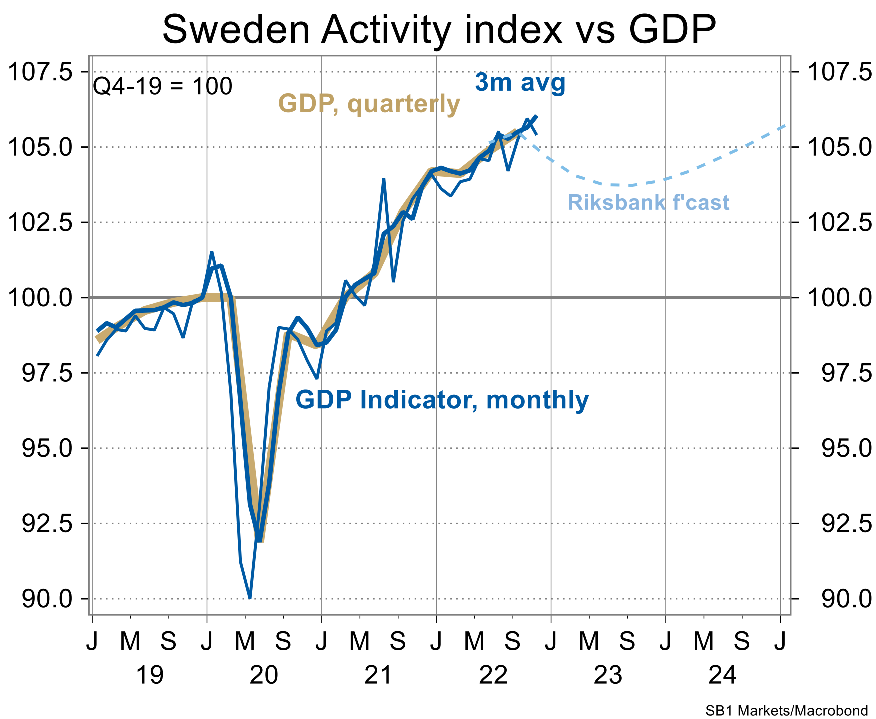


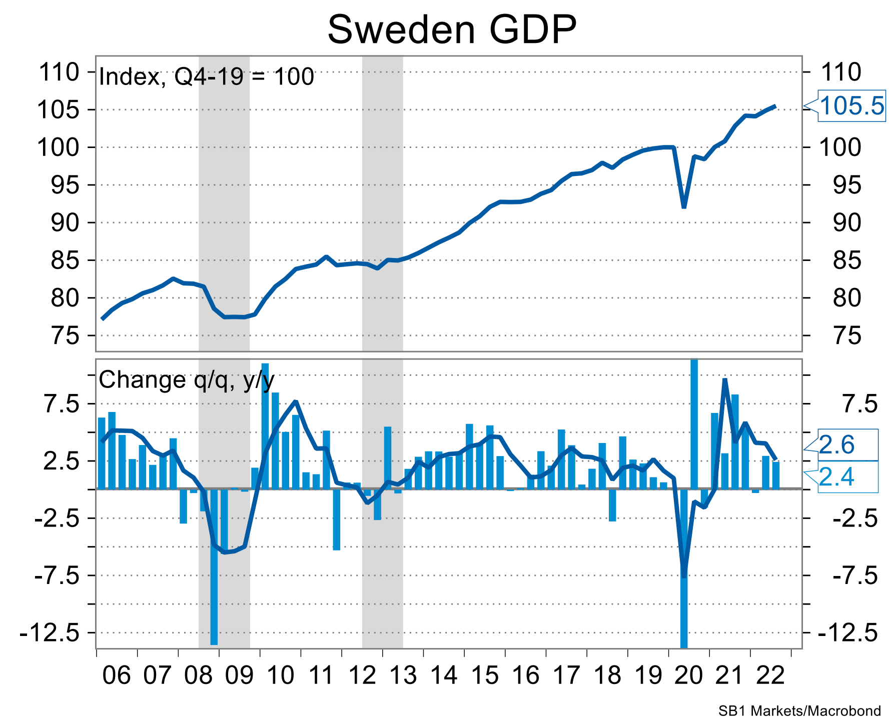


- **GDP** was expected to decline by 0.3%, following the 0.5% increase in October (which was also an upside surprise)
  - **GDP** is at the same level as before the pandemic – that is 3 years without growth. Like in the US the labour supply has contracted somewhat (while it has exploded most other places)
  - **Unemployment** it the lowest in decades, and wage inflation has climbed sharply. Inflation is above 10%, the highest since the early 80s
  - So: Not the best-balanced economy on earth
  - **Bank of England** expect GDP to contract by some well above 2% from the current level through 2023 – and slightly more into 2024. A 0.3% is expected in Q4, so far that does not seem the become the outcome, rather a minor increase
- **Mixed between sectors:** Trade the big loser through 2022, together with manufacturing. Most other sectors are trending up

Swedish GDP fell by 0.5% in November, trend is still upwards

Q4 is heading for a far better print than the Riksbank assumed in late November

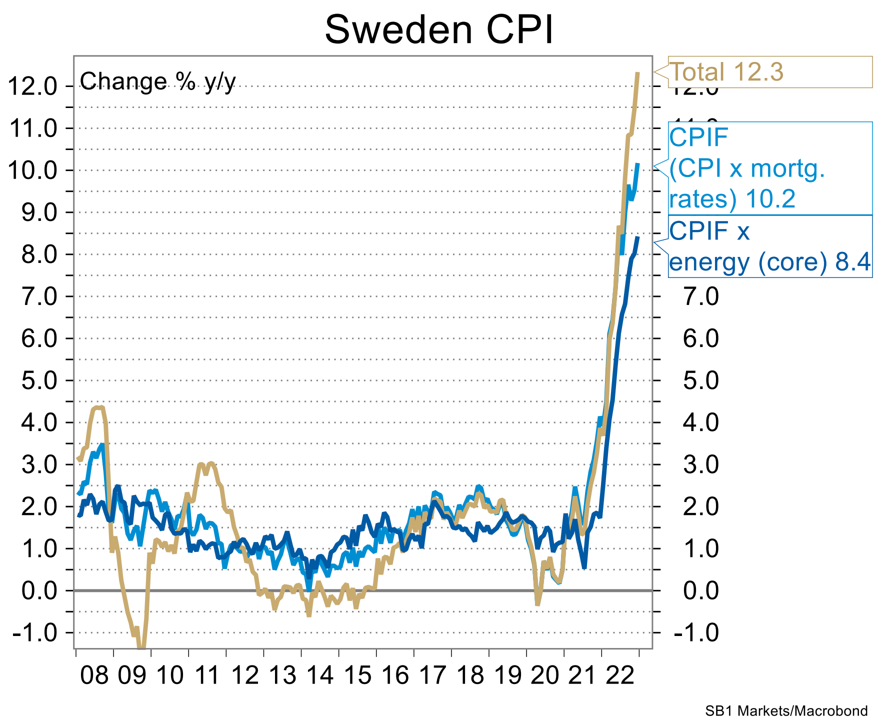


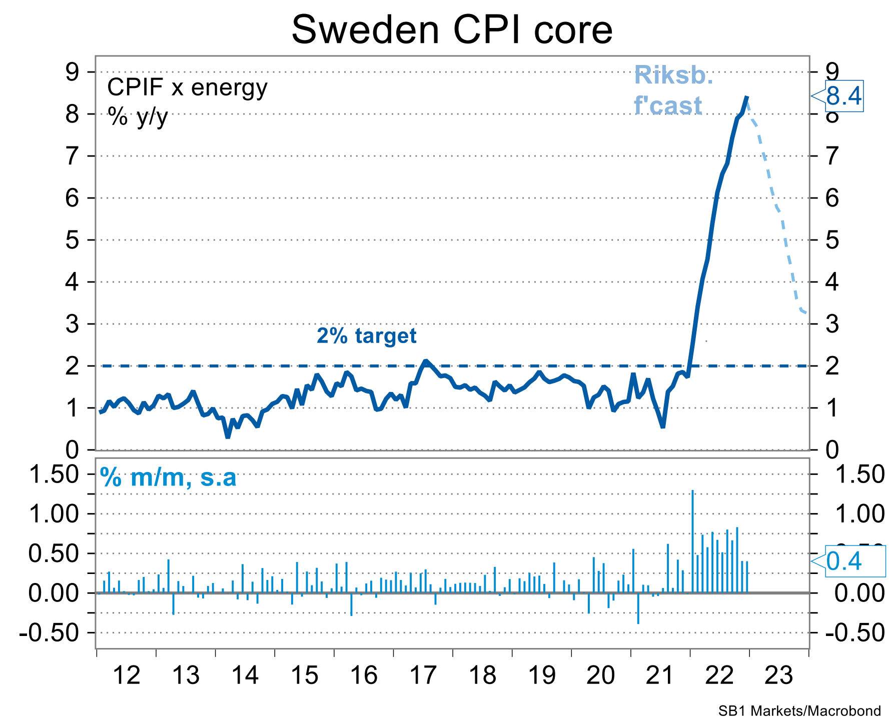


- **December data &** revisions may change the picture, but so far GDP is heading for a 0.6% growth rate in Q4 (2.4% annualised, like in Q3), assuming zero growth in December
- **In late November, the Riksbank meeting** expected a 0.8% decline in Q4 (-3.2% annualised)! In addition, it turned out that Q3 was better than assumed. Not an argument for lowering the banks interest rate path?
- **However, the outlook** is weakening, according to Swedish companies. The KI (NIER) business survey (consumer confidence not included) has fallen to below an average level but is still signalling a slight growth in GDP. The Riksbank assumes a 1.3% decline in GDP to Q2-23 from Q3 last year

Up, up – total CPI inflation up to 12.3%, 0.3 pp higher than expected

Core inflation at 8.4%, 0.1 pp above consensus/Riksbank. The only positive: Core m/m has come down to a 5% pace…

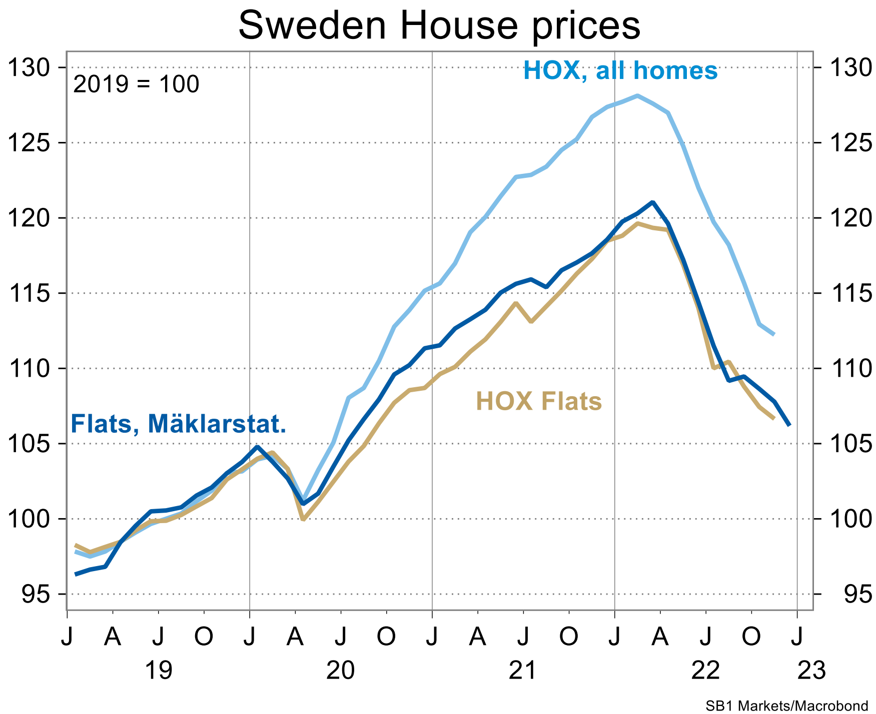


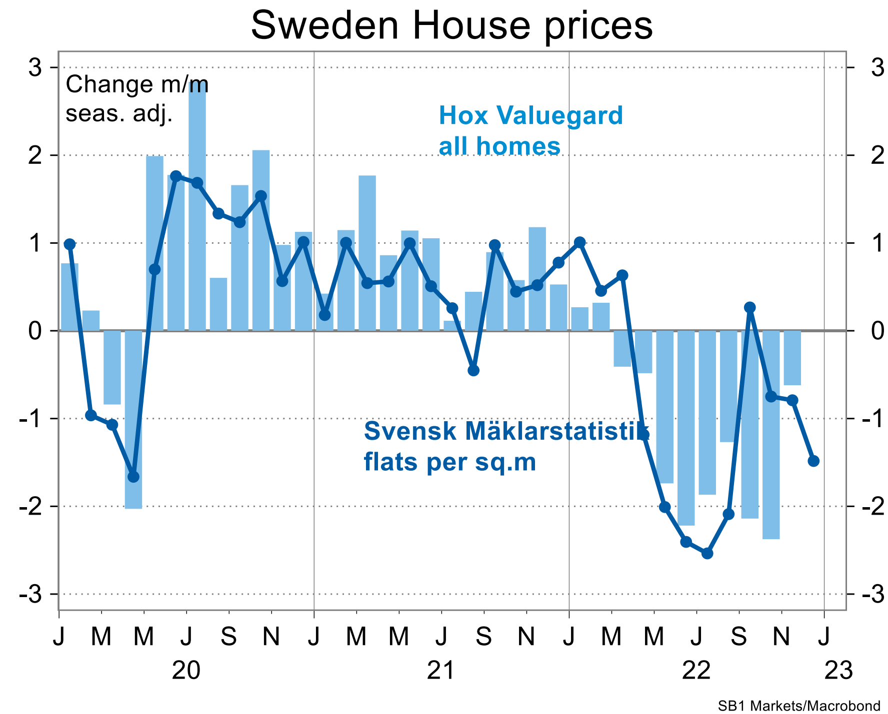


- **CPI-F x energy** (CPI-F is CPI ex mortgage rates), the 'real core', rose 0.4% in December (seas. adj). The core rate has accelerated sharply recent months, to 8.4%. **Food prices** are included in the core, and they are up 18.2% - eighteen point two per cent – y/y, lifting the core more than 3 pp. Thus, the real core is some 5%, more in line with other countries
- **Electricity prices** shot up in December, and are up 41 y/y. Including gasoline/diesel, energy prices lifts the CPI by 2.7 pp. In January, the electricity bill will decline substantially
- Besides mortgage rates, food & energy, several sectors contribute to the unusual lofty CPI print, like furnishings & household goods and hotels/restaurants
- Most likely, the December will turn out to be the peak for annual inflation. Core prices rose by an unprecedented 1.3% in January last year, and that trick can impossible (?) not be repeated now (the Riksbank assumes 0.9%), and electricity prices will most likely decline
- **The market expects the Riksbank to hike the signal rate to almost 3.5%, from the current 2.50% rate**

Well, the direction is still down, realtors report a 1.5% house price cut in Dec

In addition, November var revised to -0.8% from 0.%. Flat prices are down 12% from the ATH last March

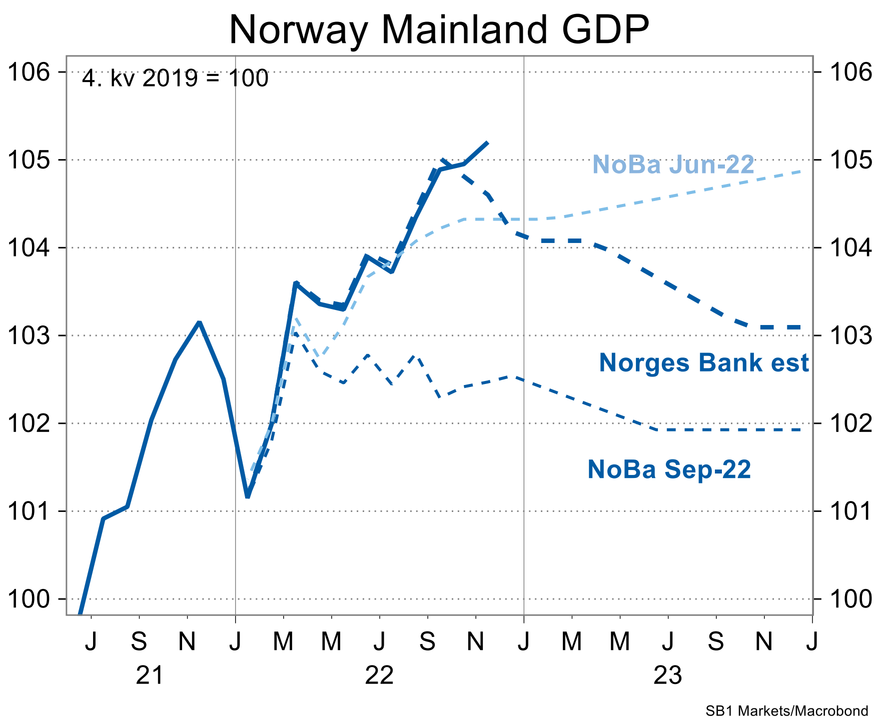


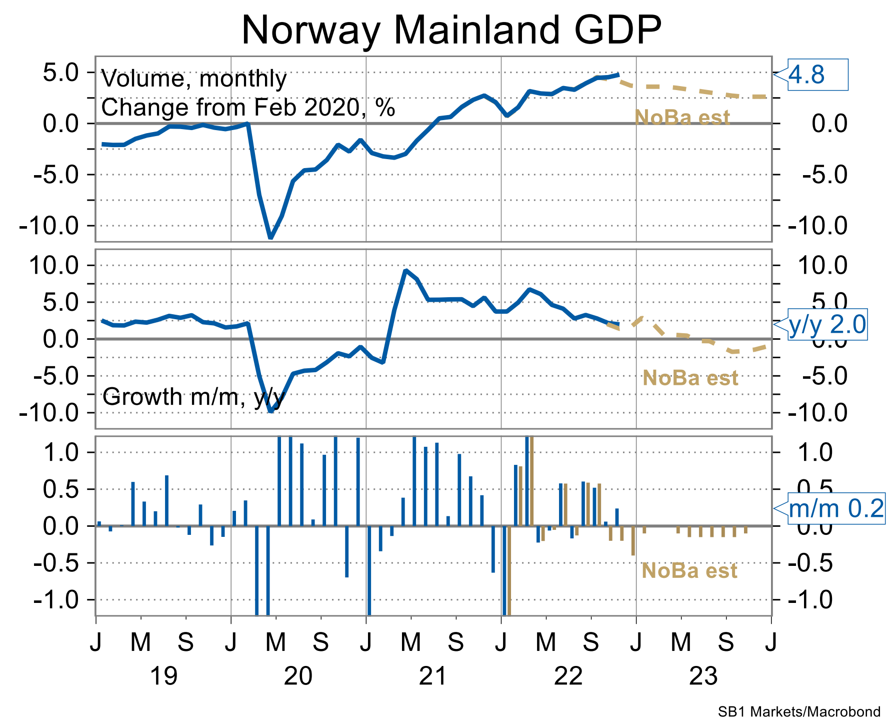


- The HOX index reported a 0.7% fall in apartment prices in November, while single-homes were down 0.8%

GDP up 0.2% in November, in line with expectations, and far above NoBa path

It won't back down: Oct revised up by 0.1 pp – and Nov GDP 0.6% higher than NoBa assumed in Dec

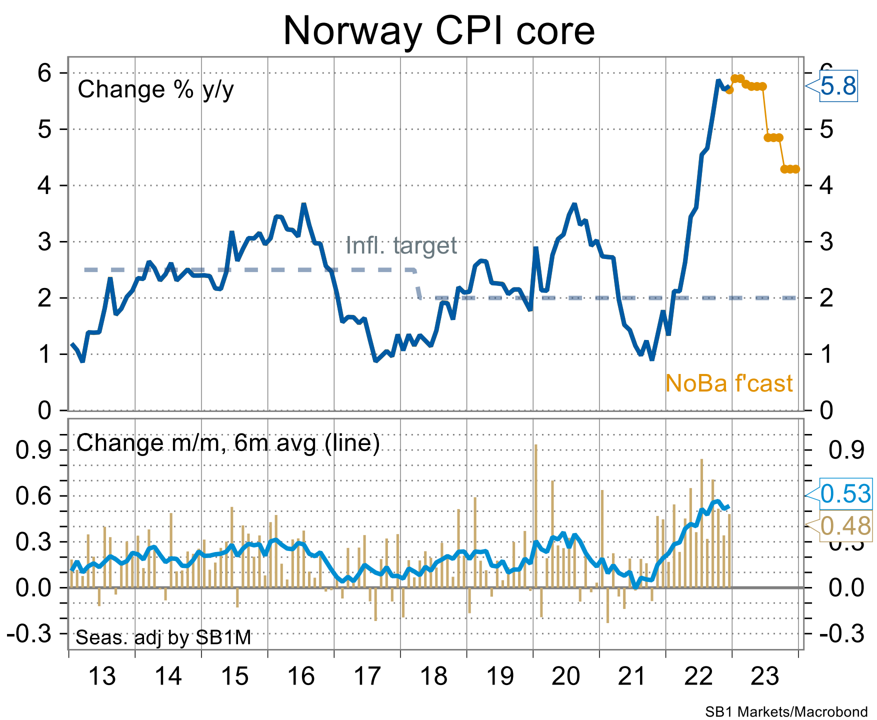




- **Mainland GDP** grew by 0.2% in November, consensus f'cast was 0.2% – 0.4% (our f'cast as the highest), while NoBa expected a 0.2% <u>decline</u>. Growth m/m in October was revised up by 0.1 pp to 0.1%.
- **Production:** Fisheries, electricity production and activity in domestic trade (car dealers were working 7/24 to deliver cars before 31/12) on the upside, manufacturing production on the downside (and more than the manufacturing production index signalled. Government value added fell by 0.1% (which explained 0.1 pp of the difference between our f'cast and the outcome)
- **Demand:** Housing and oil investments fell (we expected an uptick in oil), while ML business investments were up, but less than we assumed. Private consumption rose, broad based – but services less than we assumed. Exports fell
- **What to make out of this?** Once again, GDP has been stronger than NoBa anticipated. By itself not at argument for become more anxious regarding a 25 bp hike in the signal rate in March, which so far has been the Bank's plan

Headline inflation lower and below consensus in Dec, but the core was higher

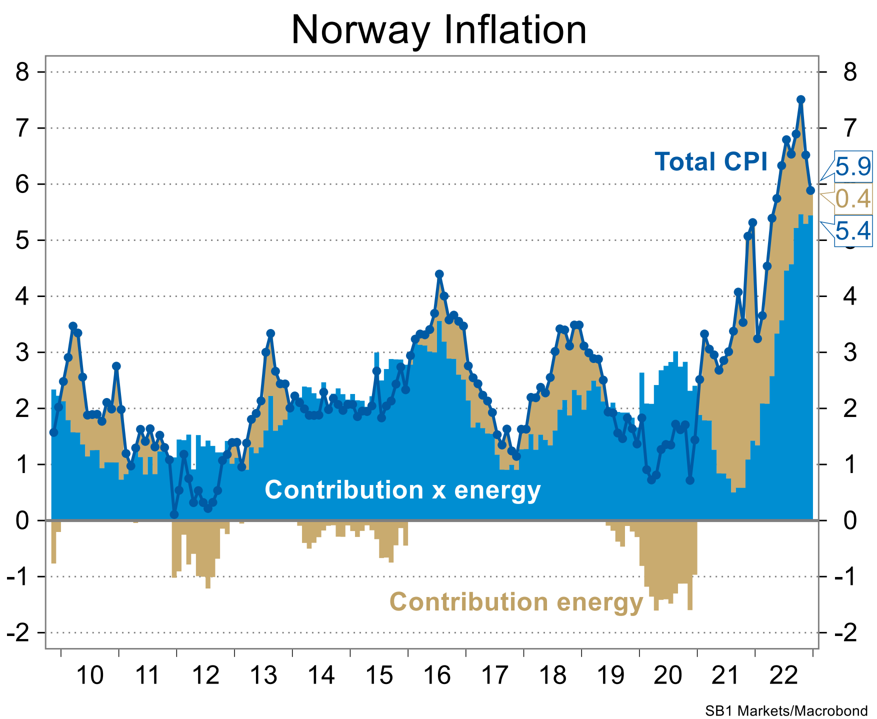
The core index 0.1 pp to 5.8%, consensus & NoBa at 5.7%. 58% of the CPI components are up more than 5%



- The **headline CPI** slowed to 5.9%, from 6.5%, as we expected. Consensus was at 6.1%, and NoBa at 6.0%. The decline was greeted as good news (and lower inflation is) but the details were not favourable:
- **CPI-ATE** (ex. energy and taxes) rose 0.5% m/m (s.a) in Dec (we expected 0.3%), and the annual rate fell accelerated 0.1 pp to 5.8% we expected 5.5%, consensus & NoBa expected 5.7%
  - **What lifted the core**: PC/TVs, cell phones & textiles, all imported goods. However, of the past year, the lions share of the 5.8% rate of inflation is due to domestically produced goods and services (influenced by imported goods prices and energy, we guess)
  - **Imported prices** are up 6.4% y/y, domestically produced goods/services 5.8%
  - **Food prices** were flat m/m but are still up 11.8%, though just 5% above 'trend'. Prices were very low a year ago
  - **The median/underlying inflation** rate is close to the annual core rate, at 5.5% – 6%. The 6 m underlying core rate is at 6.5%
- **Energy prices** fell – and a tad more than even we expected. The **electricity index** fell 3.4% (we expected flat) even if spot prices rose 2% (due to semi-fixed contracts), while **gasoline** prices fell by 8.8% (we expected -5%)
- **The outlook**
  - **Market electricity prices** have fallen sharply recent weeks, and so will the electricity CPI component – but probably not in January (semi-fixed contracts, once more)
  - **Gasoline prices** have come down to a 'right' level, given oil/product prices – possibly no further downside (m/m), but the annual rate will collapse
  - **Core inflation** has not started slowing, but we expect that to happen during H1, due to lower goods prices. Food prices may create problem again, in February

Implications for Norges Bank and the policy rate

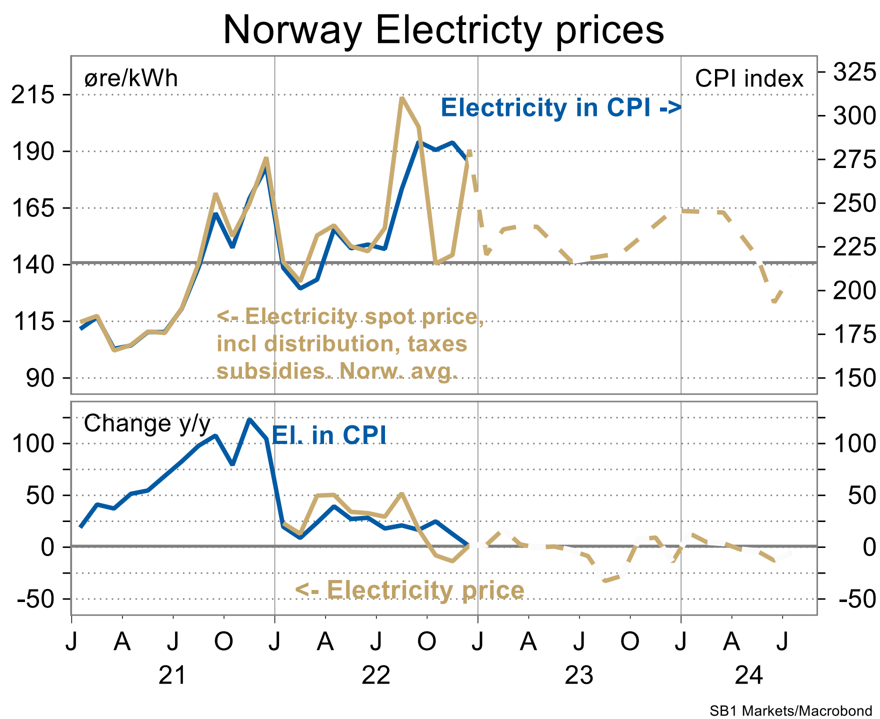
This was a bear report, not a bull report, even if the December surprise came from imported goods



- **Inflation at 5.9%, core at 5.8%, so what?**
  - **Headline inflation** has come down, but the rate is high – and it will probably turn up again in January (before falling in February)
  - **Core inflation** is also very high and higher than expected, and is not yielding – and it is still broadening
  - For **Norges Bank**, as all other central banks, wage inflation is the dominant risk vs inflation over time. So far, wage inflation has not accelerated, as we expected it would. However, as inflation will be high into 2023, there still is a risk that wage inflation will accelerate following the wage negotiations the coming spring, even if the economy is slowing.
  - In December, NoBa signalled another 25 bp hike in Q1 and possibly one more in Q2. This inflation report has not reduced the chance for that second 25 bps hike
  - Last week, markets everywhere were bullish as inflation was coming down

Finally, we got it approx. right vs. electricity prices in the CPI

The semi-fixed price contracts have created problems recent months, but we are now back on track (until further notice)



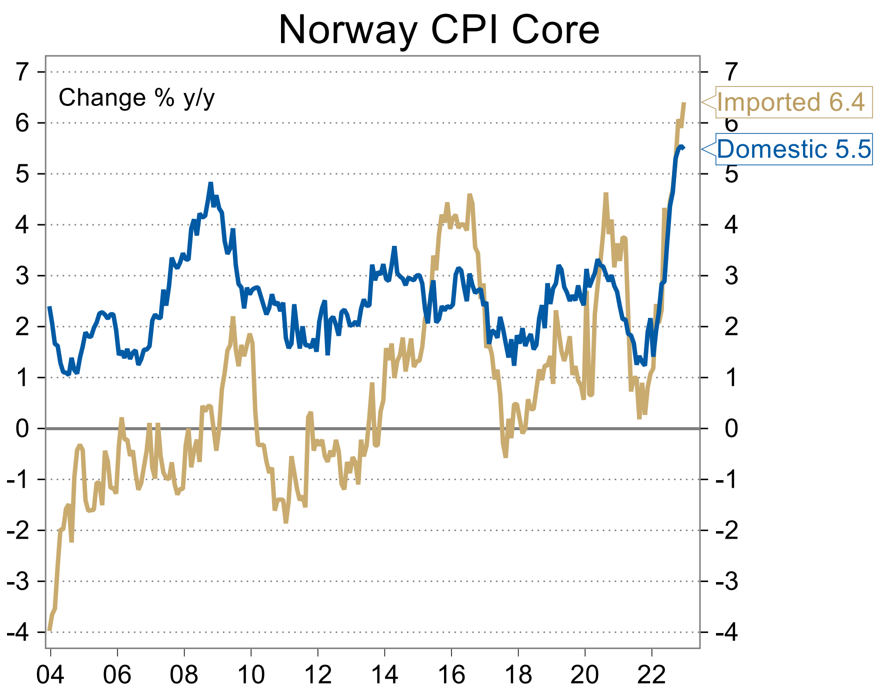
- For the rest of the year: From March onwards, current future prices indicate a zero, and negative growth rate, measured y/y

- Even if **spot prices** + transfer fees + taxes – subsidies rose by some 24%, we assumed that the average consumer price (in the CPI) would be unchanged. Why? The **semi-fixed price contracts** (1 m fix) turned out to be cheaper than the spot price based contracts better in line with the spot market, after being miles above in Oct & Nov (where our f'casts were widely off mark)
  - **Dec contracts** for the semi-fixers were based on a Dec future price at some 180 øre/kWh, while the spot turned out to be higher, at 240, and a much larger subsidy was returned to the fixers too. Thus, the semi-fixed contracts yielded a comfortable low energy bill!
- By luck and accident, we were quite correct. SSB reported at 3.7% decline
- **In January**, spot prices have once again, at least so far, fallen sharply. The average is so far 110 øre/kWh – and could end up at 100 – 150 øre/kWh, down from 240 øre in December (avg. so far 110 øre/kWh). If that was the whole story, the CPI index would have fallen some 20% – 30% m/m in January (like prices fell in Jan-22)
- However, in mid December, the semi-fixed contract prices were set based on a **January future price** around 310 øre/kWh. The **subsidy** will be limited (since it is based on the spot price which probably will be low) and the bill in January will be higher than in December for these fixers (if there are anybody left on such contracts now). That is, even if the spot price has 'collapsed' just like in October and November
  - The semi-fixed contracts have probably deemed to be less attractive recent months, and the market share of some 17% before the autumn, may now be lower. Still, as their price deviates grossly from prices on contracts based on spot prices, they have a sizeable impact on the average household price, calculated by SSB
- We assume these twists and turns will be cancelled out in February. <u>But the January CPI print will quite likely be lifted due to these technicalities. As prices fell sharply last year, we expect a positive contribution from el. prices to annual CPI growth in January</u>

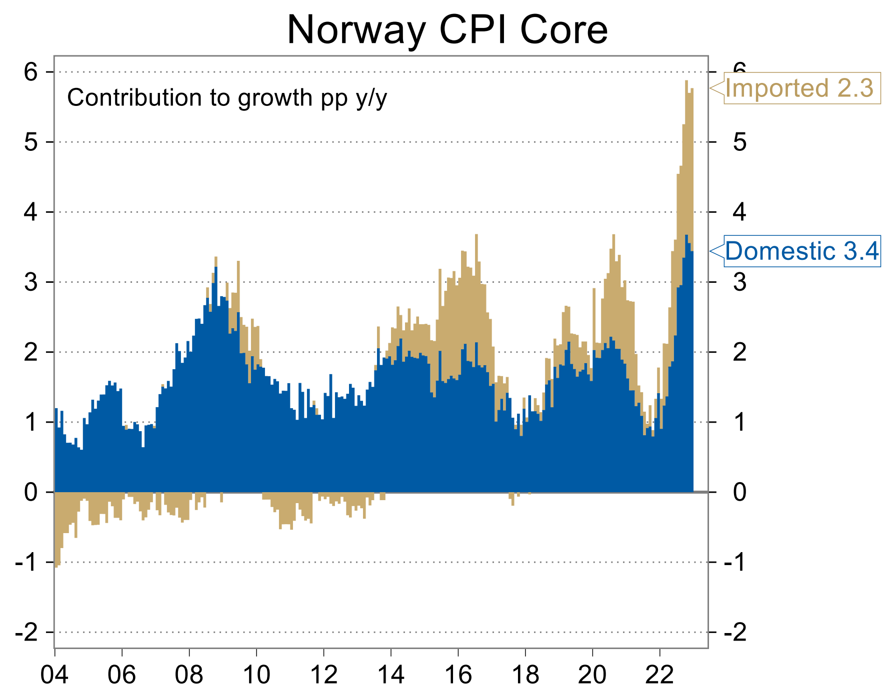
A 90% subusidy efficiency is assumed as more electricity is used when prices are high (due to low temperatures

Both imported goods and domestically produced goods & services contribute

… and the domestic component is by far the largest contributor



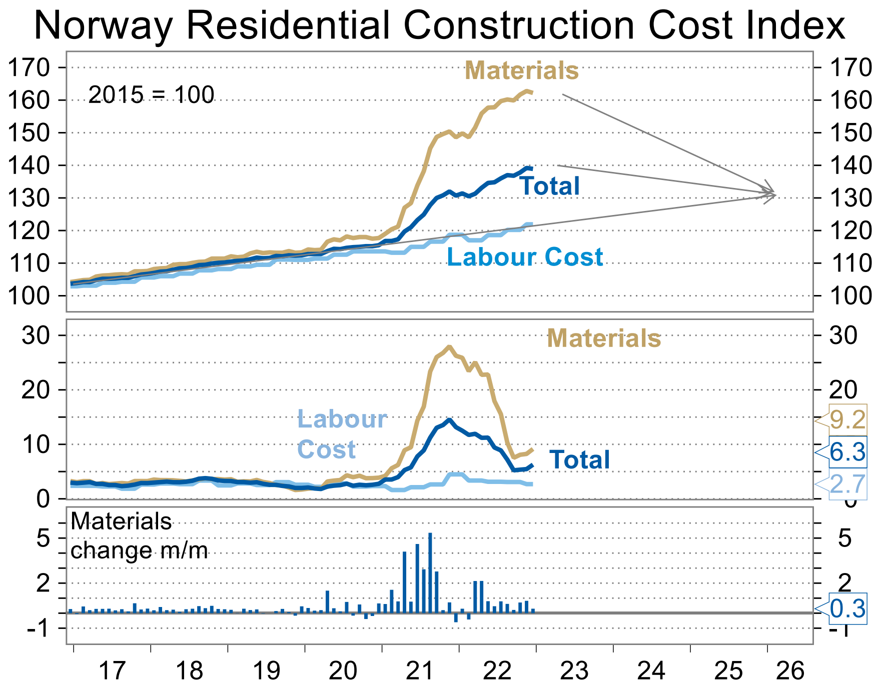
SB1 Markets/Macrobond

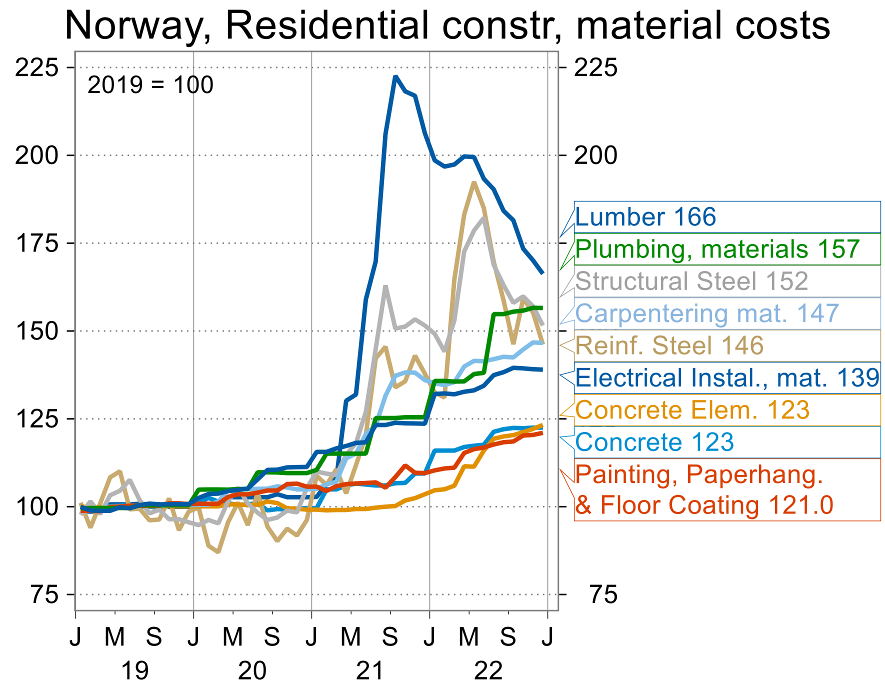


SB1 Markets/Macrobond

Building material prices still on the way up, even if lumber & steel are falling

We are quite confident, material prices will soon decline. No signs of any labour cost inflation

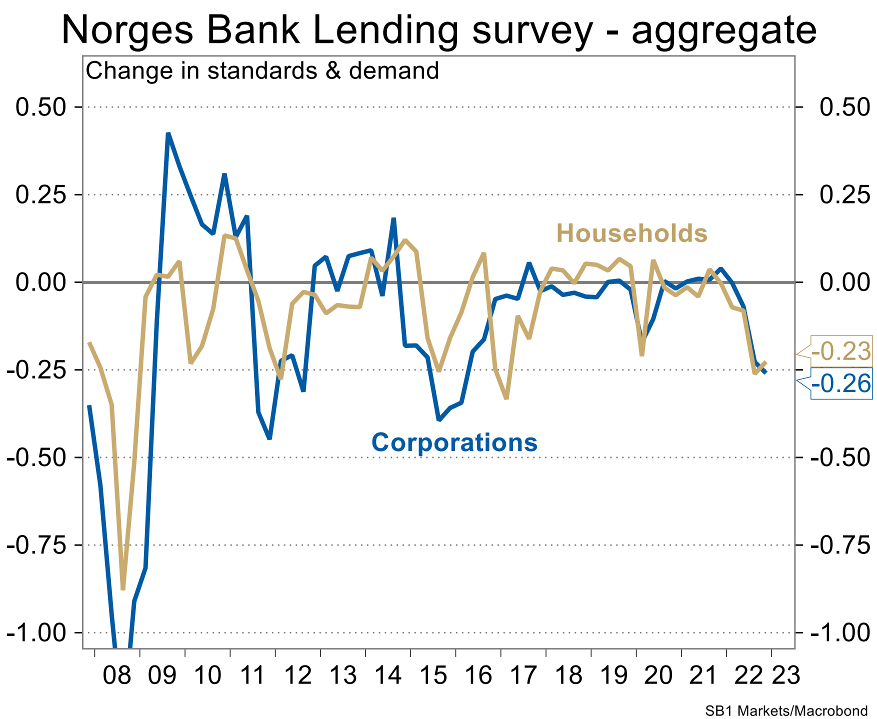


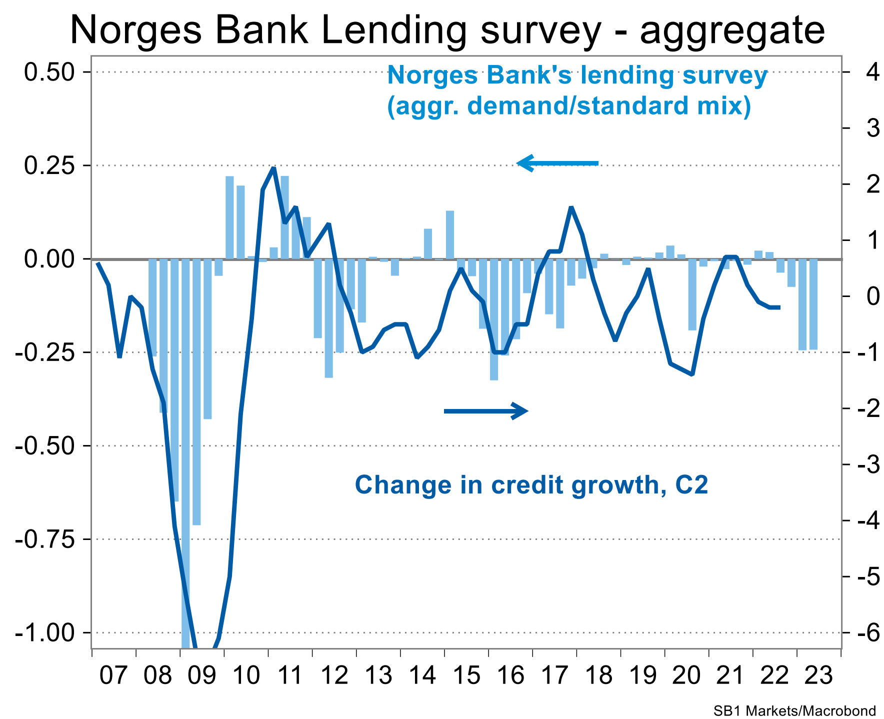


- **Material prices** (houses and apartments) added 0.3% December. Prices are up 9.2%, down from 28% at the peak
  - Lumber prices are trending down, and reports signal further declines the coming months. Steel prices also fell in December but these prices have flattened recent months (in line with global steel prices)
  - Other material prices are still trending up; but slower. Plumbing materials, electrical equipment and concreate rose just sightly
- **Labour costs** were just up 2.7% y/y in Q4, down from 3.1% in Q3 – no sign of acceleration
- Including labour costs, the **total building** cost index is up by 6.3%, down from the ATH at 14.6% at the peak last Oct. The price level is up 13% vs. the pre-pandemic 2.5% growth path. Going forward, we still think lower material costs will bring total construction costs down to more normal levels. Upside risk: A brisk recovery in the construction sector in China, pushing steel and other globally traded construction related commodities upwards

The credit cycle has turned – from the demand and the supply side

Demand is waning, both from households and businesses – but standards are not tightened by much



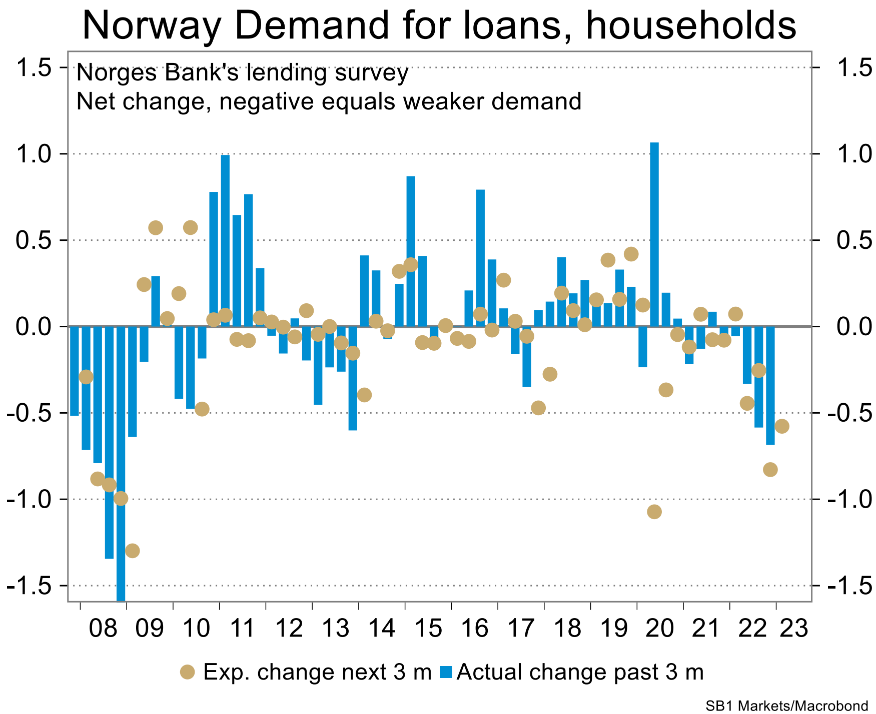


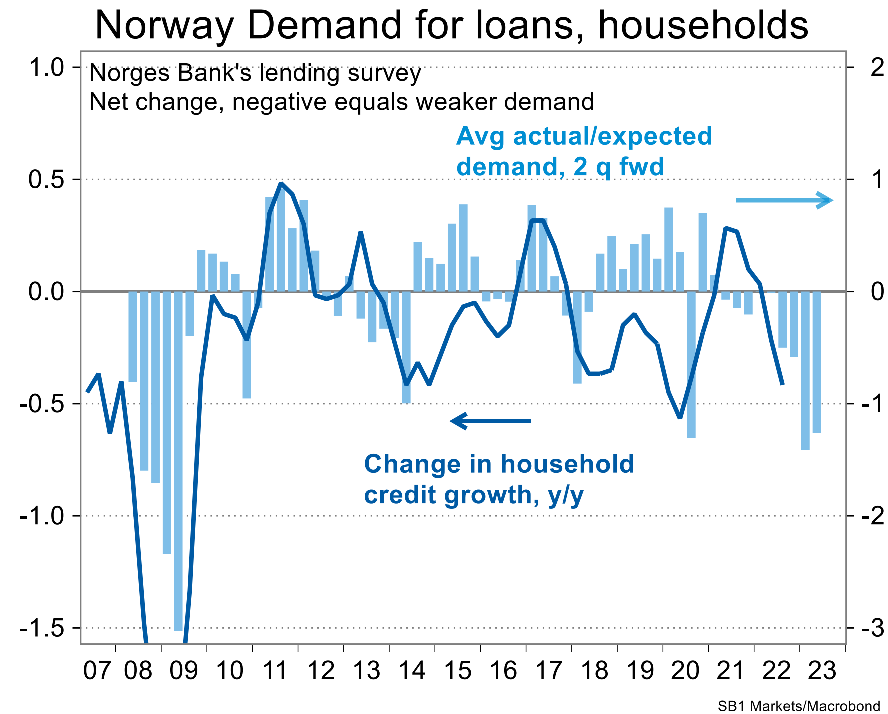
- .. And the there is sill no drama, neither vs. demand nor credit standards - according to Norges Bank’s lending survey among banks

Data in this section are seasonally adjusted

Demand from households weaker in Q4, as was expected…

…and the negative trend is expected to continue into Q1



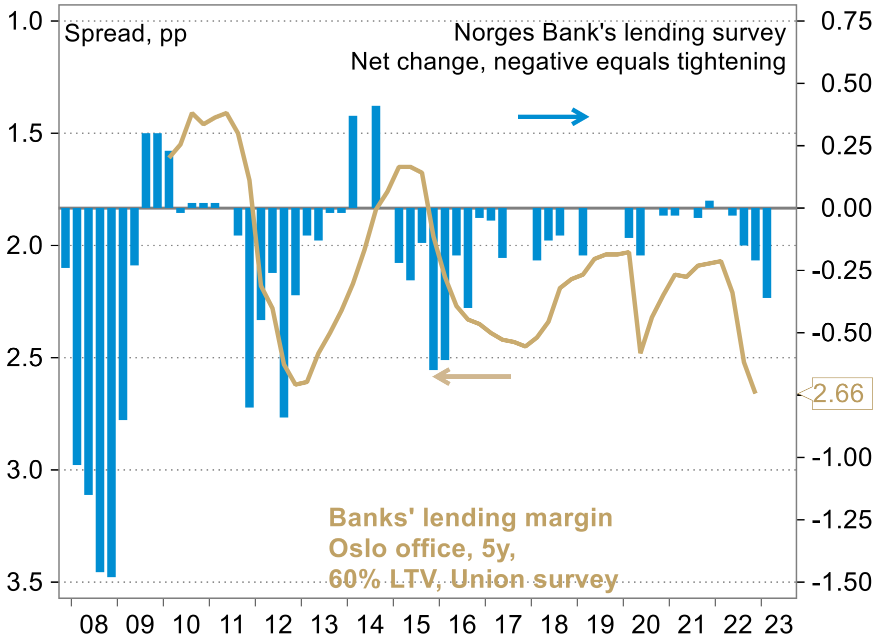


- There is not any tight correlation between banks' expectations for household demand for credit or their assessment of actual growth and the realised growth in household credit, as measured by the C2 credit indicator
  - Still, the lending survey probably tells the sentiment among bankers pretty well
  - The reported decline in demand the past two quarters as well as the expected decline in Q2 is not as harsh during the worst of the financial crisis (2008), but barring that period – when growth in household debt fell to 7% from 13% - the 2nd toughest change in bankers' assessment

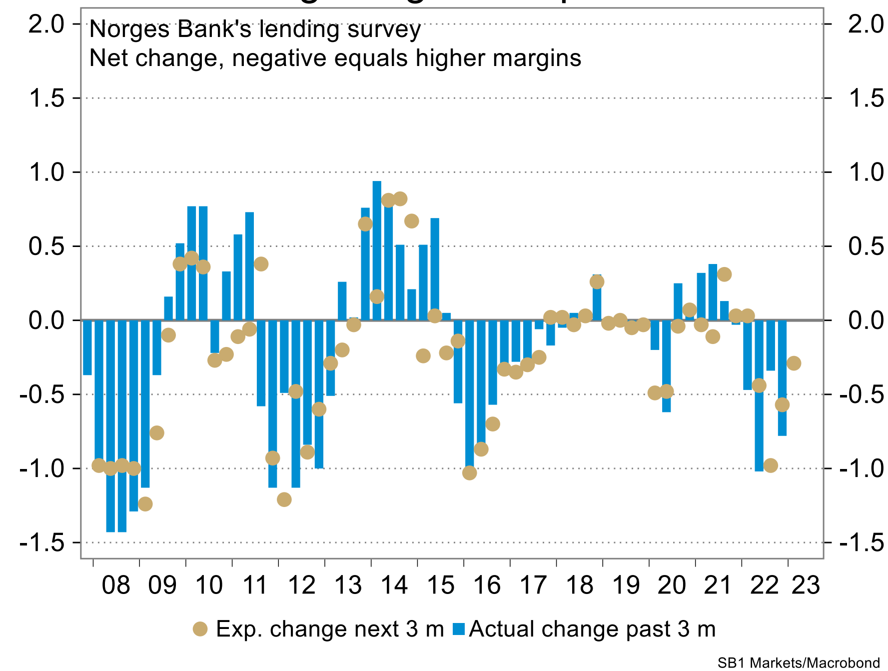
Tighter standards, higher margins vs. real estate + higher margins vs. all corps.

Banks increased their lending margin vs. businesses in Q4. More to come in Q1

Credit standards commercial real estate

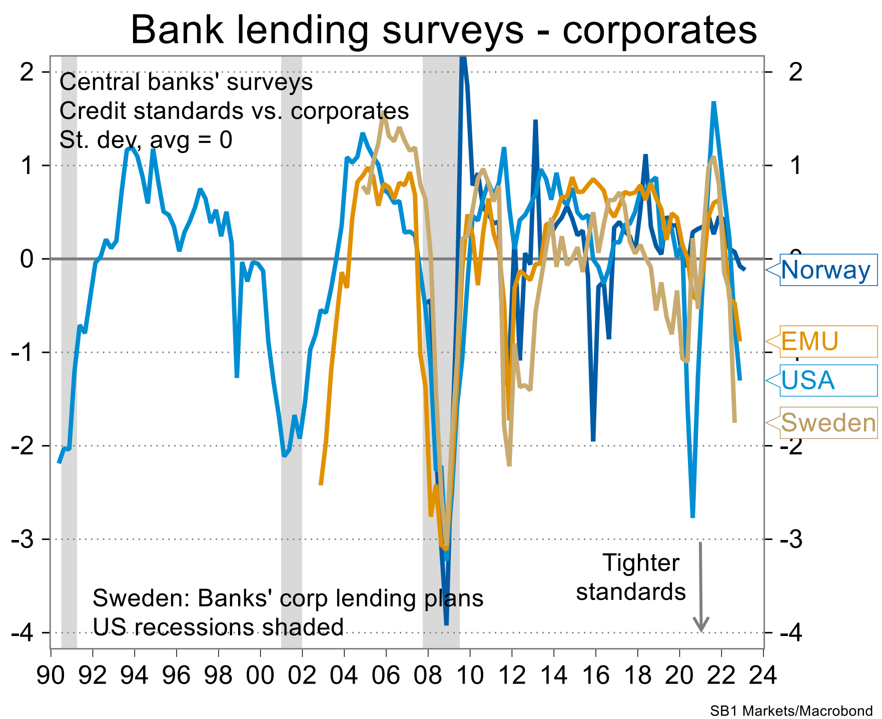


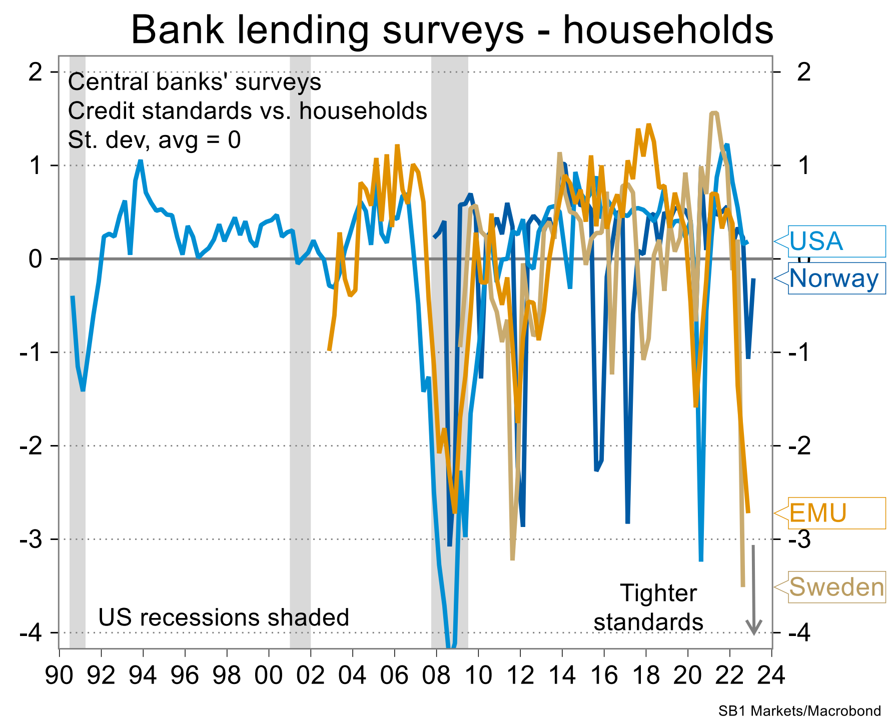
Lending margins Corporations



Global view: A substantial tightening everywhere – barring Norway??

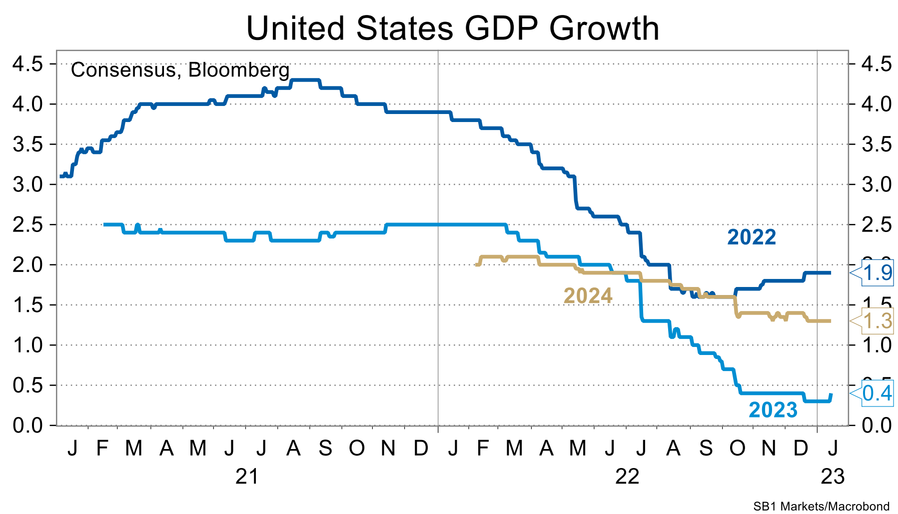
Norwegian banks an outlier? Seems so. Some tightening but nothing when compared with ROW. Rather surprising

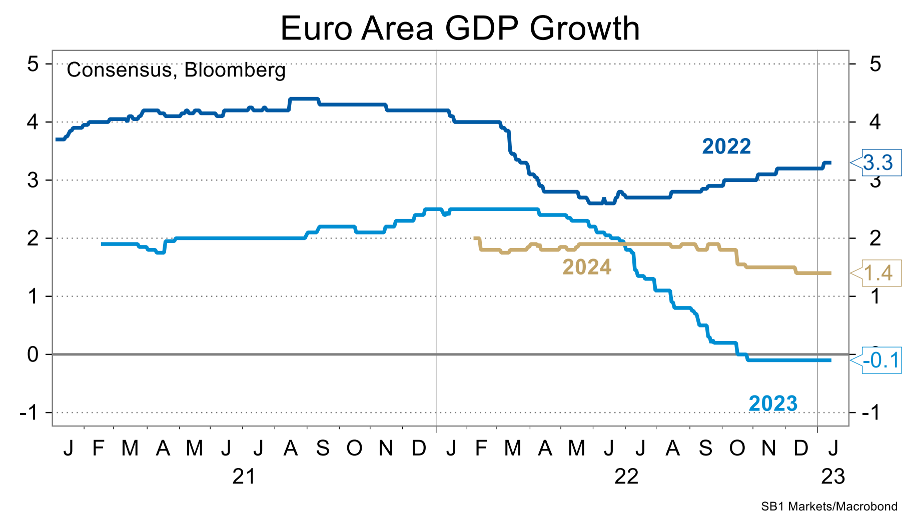


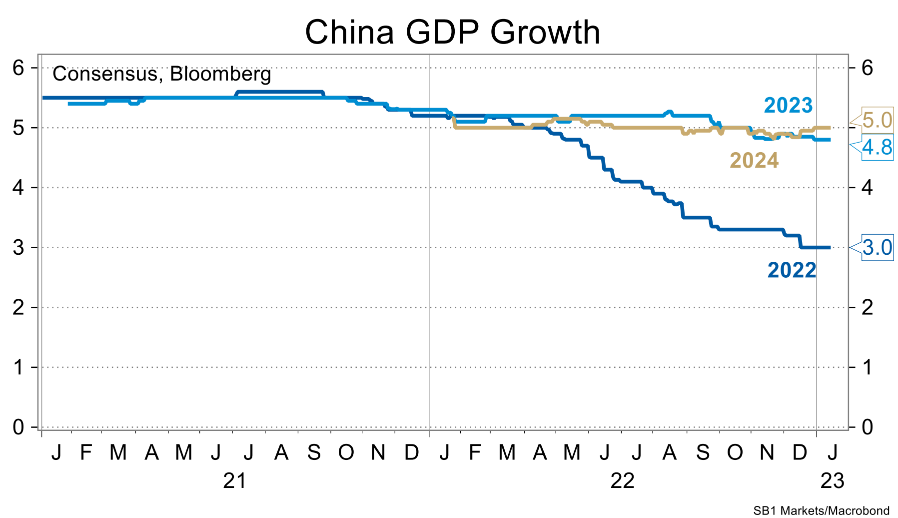


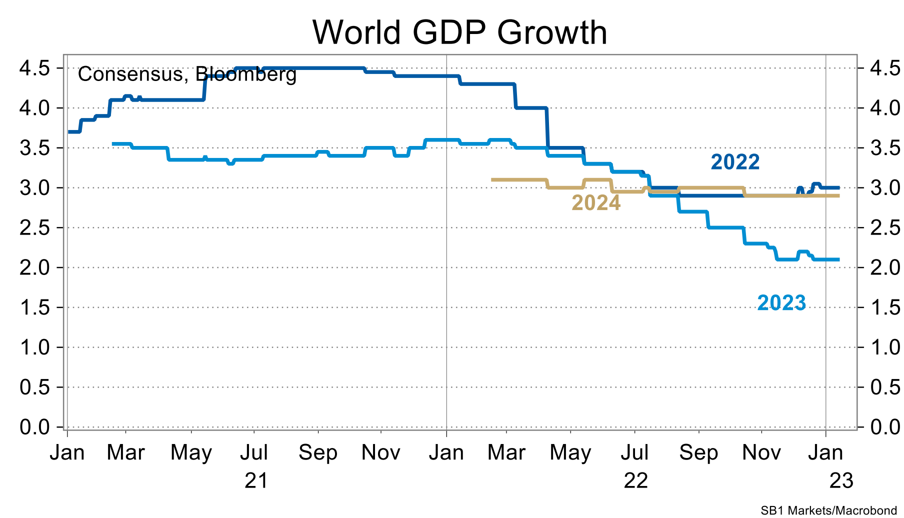
The first 2023 upgrade: US GDP growth revised up to 0.4%!

The 2023 f'casts imply a short and shallow recession in the US next year, and somewhat deeper one in Europe



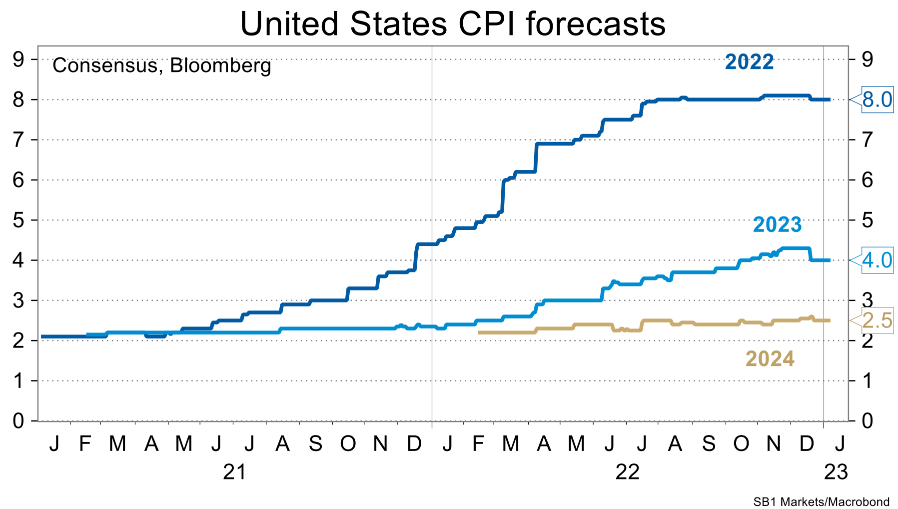


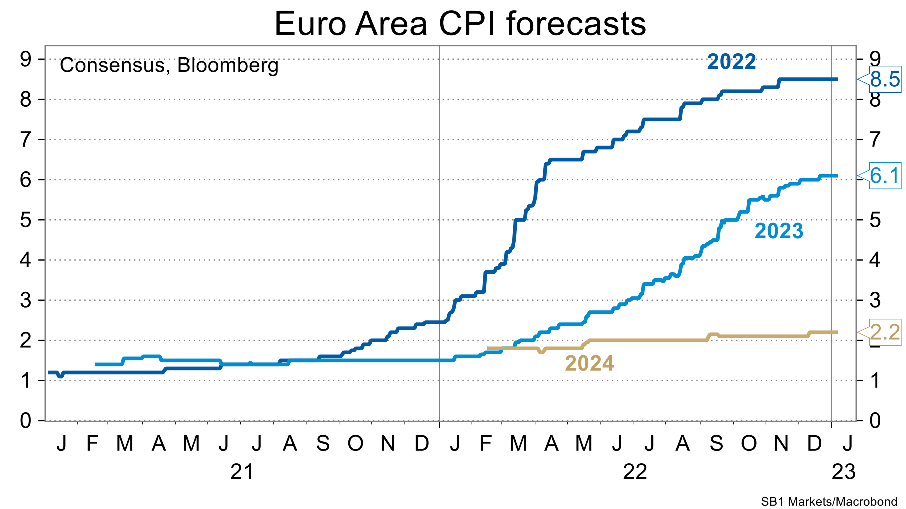




US 2023 inflation expectations have peaked, EMU soon to follow?

While inflation expectations in the EMU rose a tick last week, to 6.1%. Given the decline in gas prices, too pessimistic??

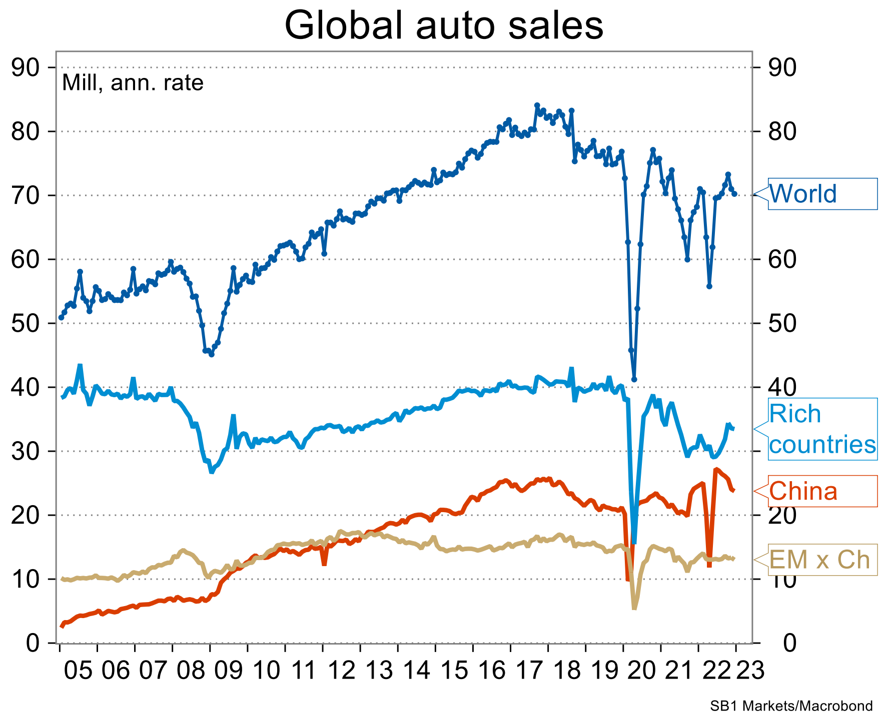


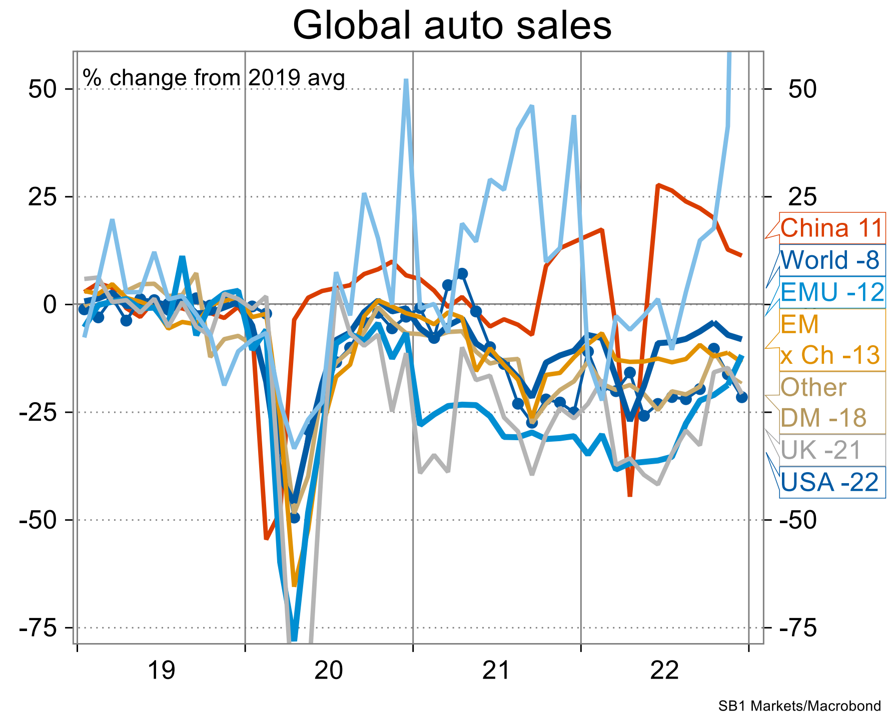


SpareBank 1 MARKETS

Global auto sales further down in December, just EMU (and Norway) up

Sales declined in US and China – as well as in the average of EM x China, due to a decline in India



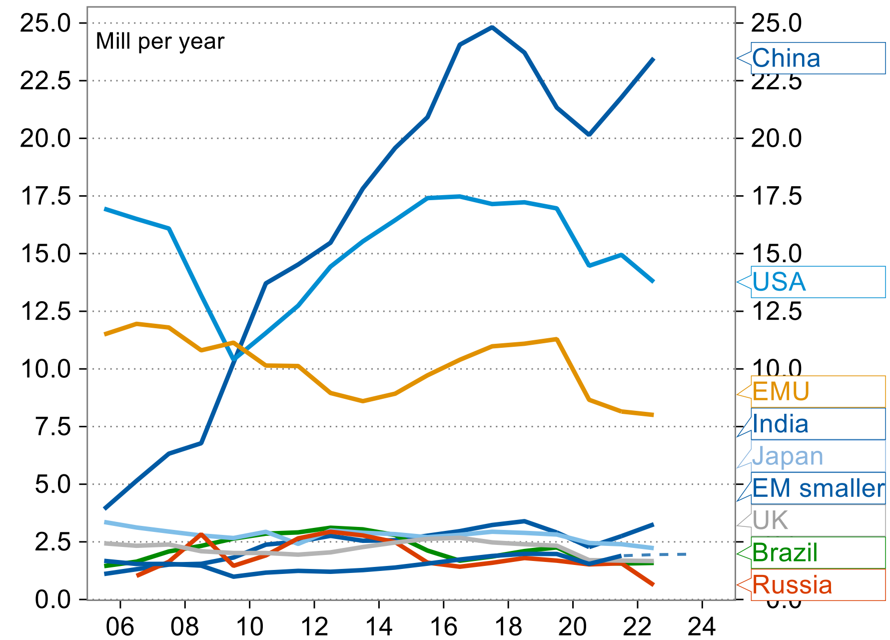


- **Global auto sales** fell 1% in Dec. Sales have been rather stable recent through H2, and are 8% below the 2019 level. However, 2019 is an easy comparison: Sales are down almost 15% from the peak in 2018 and 30% below the pre-2018 trend growth path!
- Sales in **China** fell further, but are still 11% above the 2019 level, even if housing is struggling (sales are still lower than in 2017). Sales in the **US** fell m/m and are down 22% since 2019. **EMU** sales continued upwards, primarily due to a surge in German sales, and EMU sales are 12% below the 2019 level. **UK** sales declined, and are down 21% from 2019! **Norwegian** sales were record high
- Sales in **EM x China** fell marginally, due to lower sales in India (but the level is high). Russian sales remain depressed
- **Auto production** has been the limiting factor, at last since late 2020. Now, the market balance is clearly better, and in the UIS we suspect demand to slow as well. Production has increased most places, and is higher than in 2019 some places.
  The US is just marginally below

China the winner in 2022 – and the largest market, by far

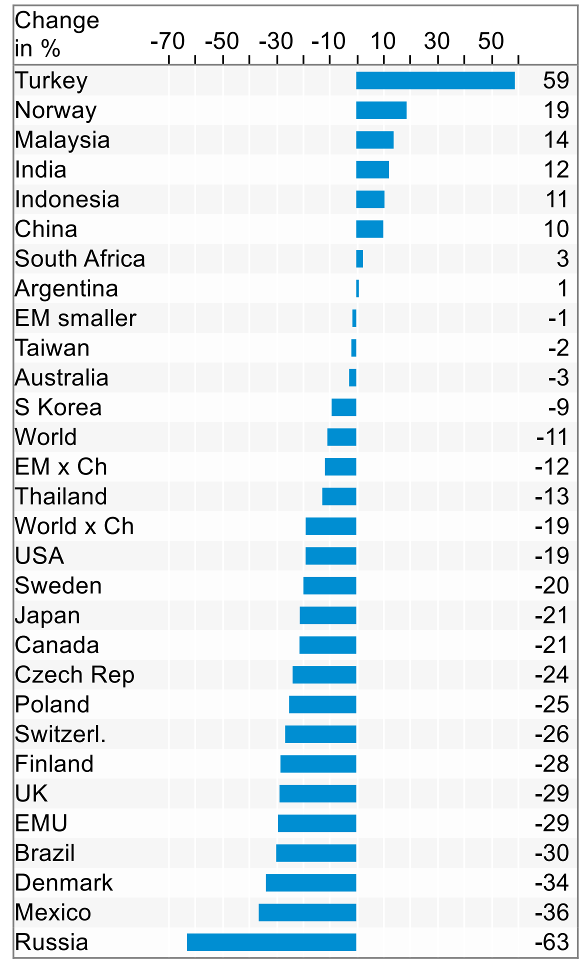
However, Turkey and Norway (!) saw the largest increase from before the pandemic!

Global auto sales



SB1 Markets/Macrobond

Auto sales 2019 - 2022



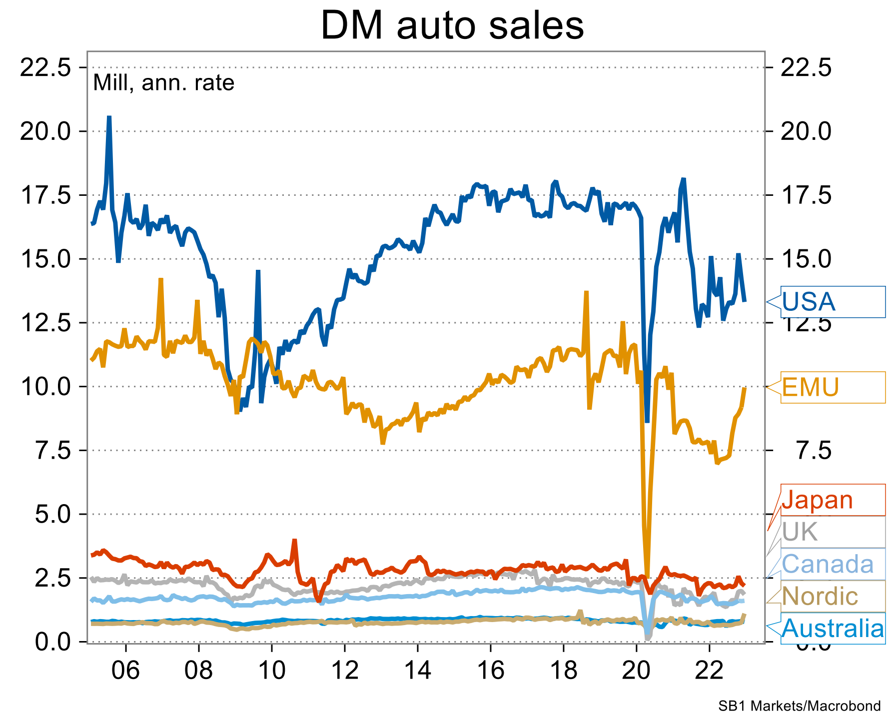
SB1 Markets/Macrobond

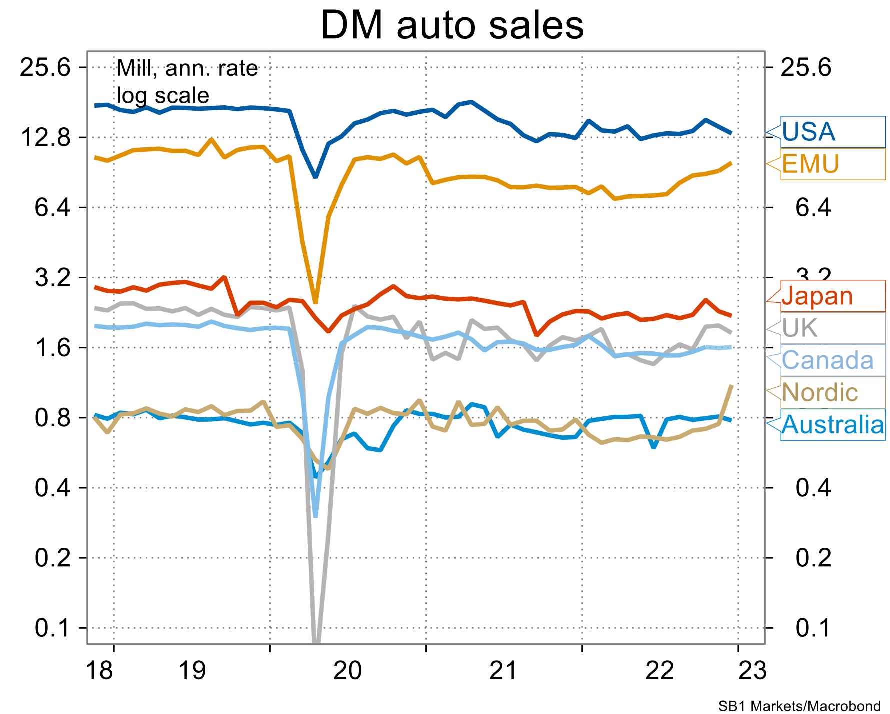
- **Global auto sales** were unchanged in 2022 vs. 2021. China contributed on the upside, US and Russian most on the downside
- From 2019:
  - **China** is up by 10% - but remain below the 2018 level.
  - **Indian** sales are up 12%. Russia is down 63%, at the bottom of the list
  - Most rich countries are down, by 19% in the **US**, 21% in **Japan**, while **EMU** and **UK** is down 29%
  - **Sweden** is down 20%, **Denmark** 34% - and **Norway** is up 19%

SpareBank 1 MARKETS

DM sales: Sales trend up, even if inflation is high, interest rates are soaring

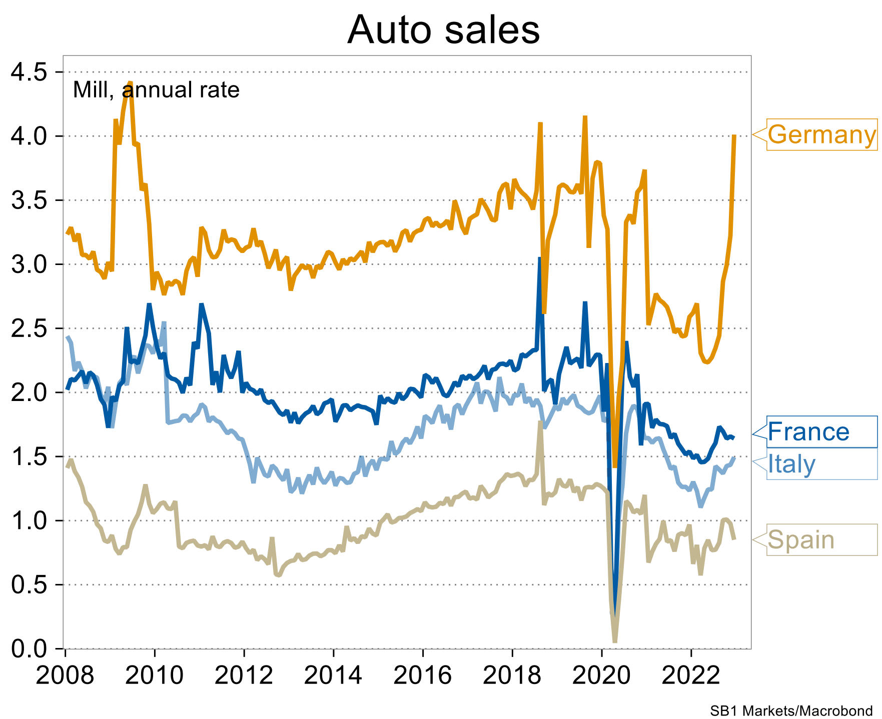
… as supply of new cars strengthens

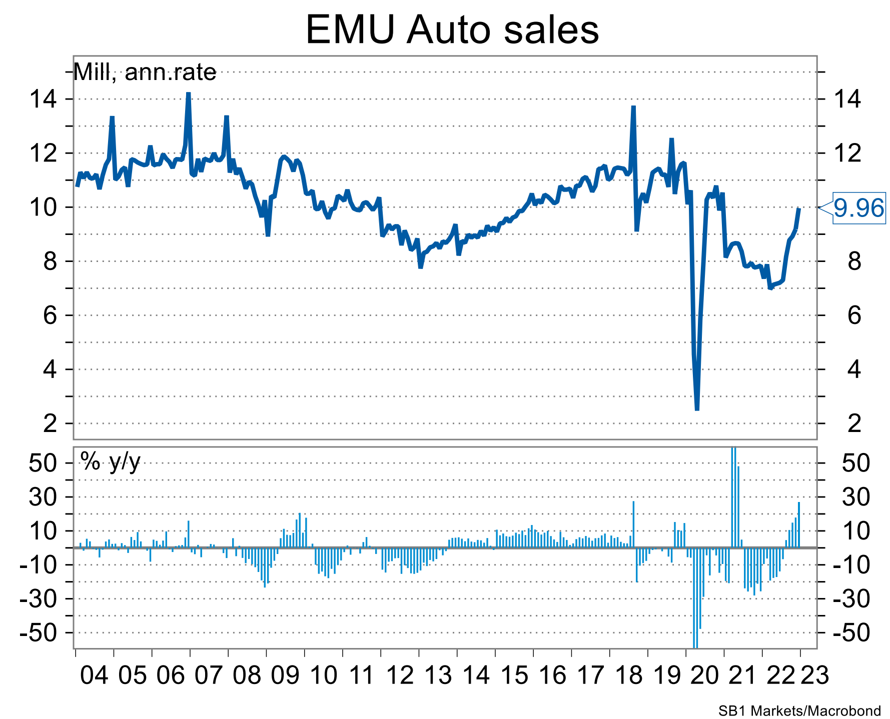




EMU: One of the best months ever, in Germany

Some tax changes, but they do not seem to explain the huge lift in December (or the 80% lift from last May)

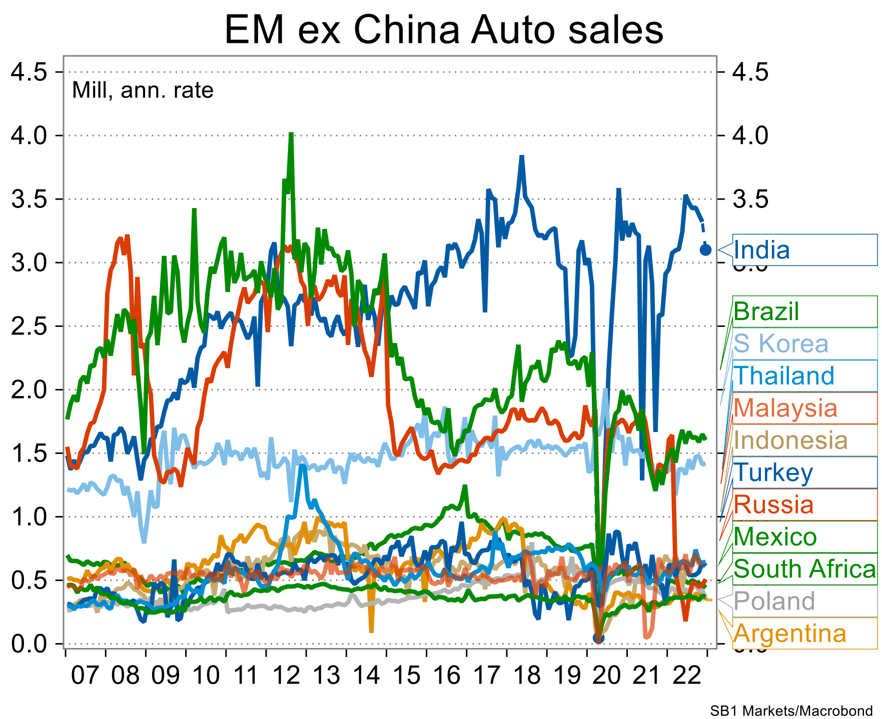


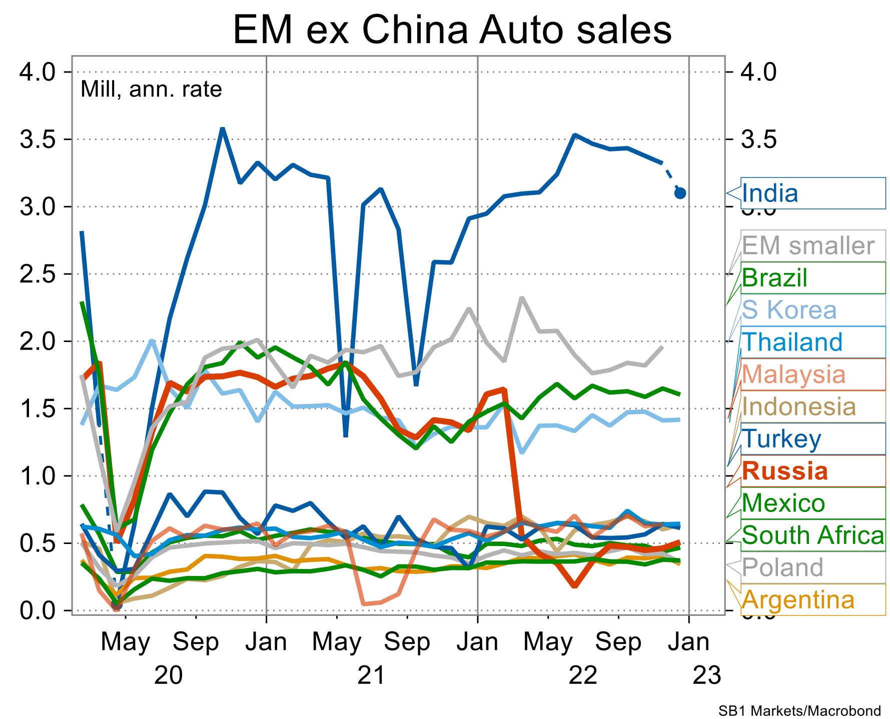


- Still, we doubt German auto sales will remain at the 4 mill/y level the coming months
- Small changes in auto sales/new registrations among other EMU countries reported so far – and all are way below pre-pandemic levels

EM: some flattening through last year, and several countries well below ATHs

Brazilian sales are cut in half (vs. 2012/13 level) – and Russian sales were once upon a time 6 times higher than today



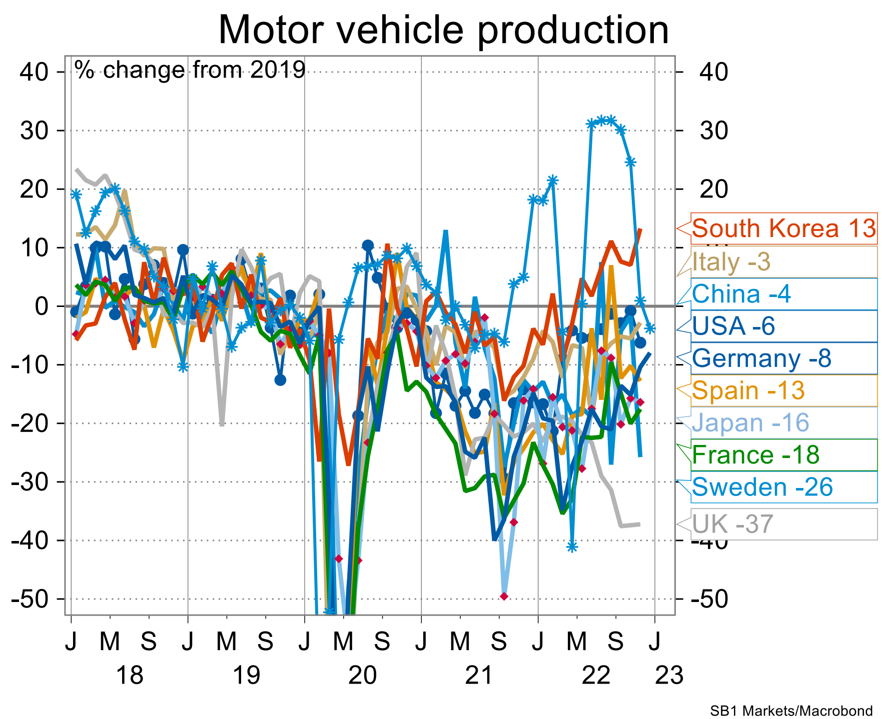


- Indian sales are still close to ATH levels (the Nov. data point is based on media reports, and is uncertain)
- Sales in EM x China & Russia are just marginally down vs the 2019 level

Not all countries have reported yet, and for some countries we have just plugged in figures from media reports that are not always correct

Auto production is gradually recovering

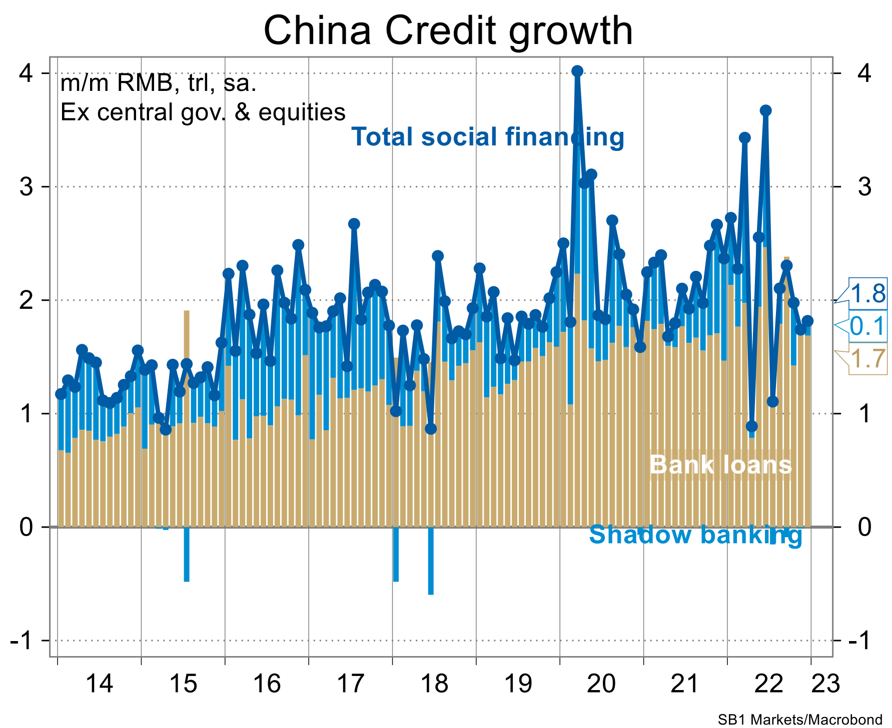
However, somebody hit the brake on Chinese production in Nov/Dec. We think we know why

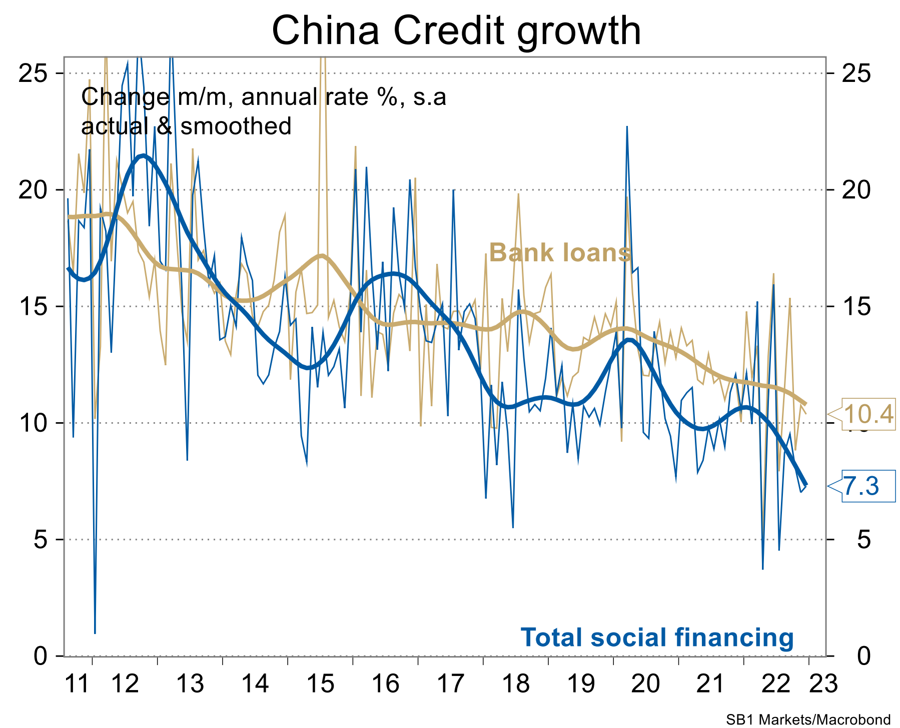


- However, Chinese production remains 3% above the 2019 level

Slow credit growth in December too, and the trend is down

Covid, or a real ‘crunch’? We will soon find out ☺

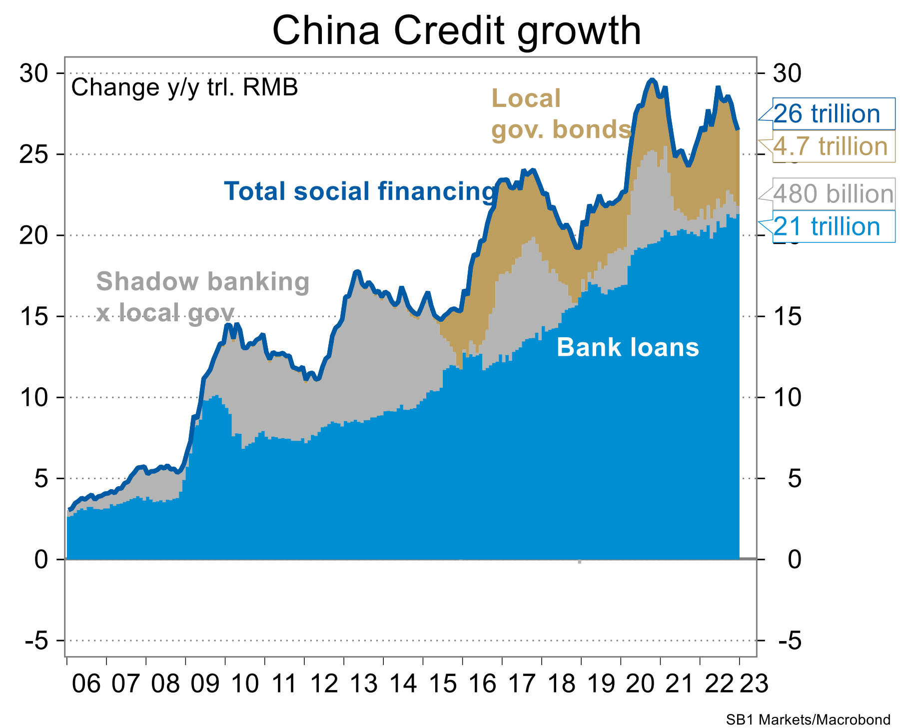


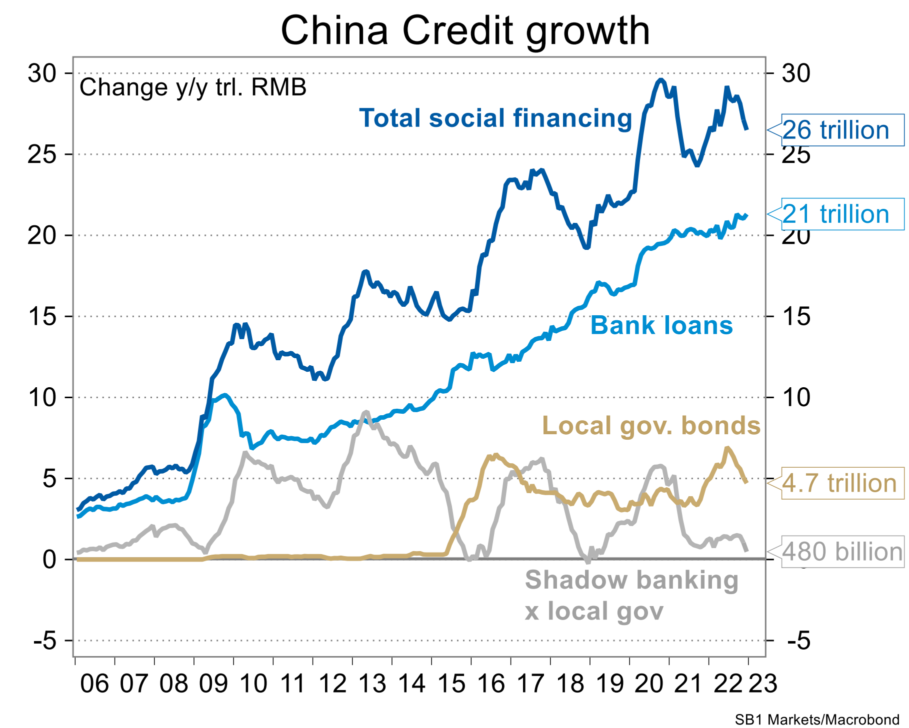


- **Core total credit** (social financing, ex central gov bonds, equites) grew at a 7.3% pace in Dec (m/m, seas. adj. annualised), up from % 7.0% in Nov (we initially assumed 7.7%). The trend is steeply down. The annual growth rate fell 0.3 pp to 9.5%
- **The official total social financing** rose RMB 1.0 trl, expected 1.6 trl. Our core credit supply grew RBM 1.8 bn (s.a.), marginally up from Nov
  - **Bank loans** rose by RMB 1.7 trl (s.a) or at a 10.4% annualised pace, well <u>above</u> expectations (actual 1.4 trl vs. exp 1.2 trl) . Loans are up 11.6% y/y
  - **Shadow banking credit** (all sort of credit outside banks) rose by just RMB 0.1 trl, and is up 5.3% y/y – but just 0.7% excluding local gov. bonds
  - **Local governments have been** responsible for most of the increase in credit outside banks over the last year , but growth has slowed recent months (including our Dec est., no data published yet)
- **Authorities** have announced several measures in order to stimulate the economy (and signalled that more will come), some directed towards the credit market, mostly to support the struggling construction sector

Credit growth is slowing, will the accelerator work this time too?

The authorities have turned expansionary, also vs. the construction sector – which needs funding support

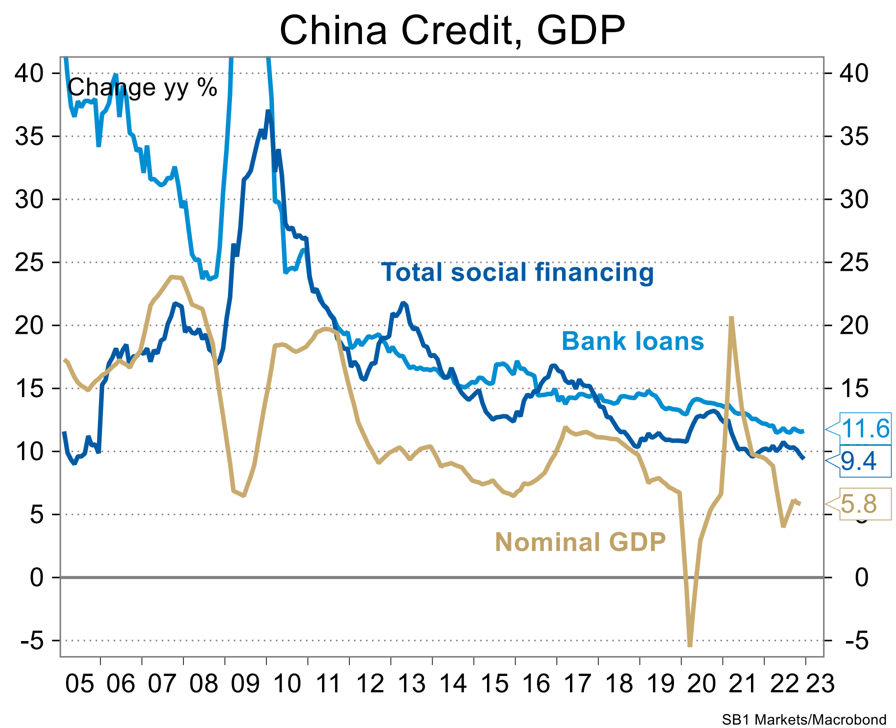


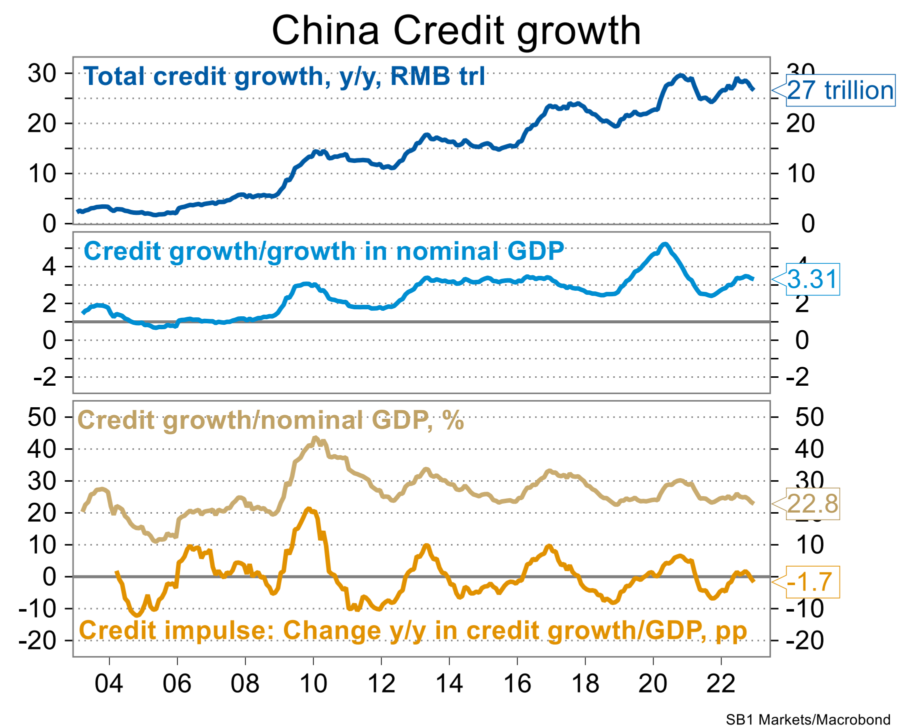


- Over the past year, **total credit** has expanded by RMB 26 trl, equalling 23% of annual GDP, up from the 24 trl at the last bottom in Sep-21 but still down from almost RMB 330 trl at the peak in 2020, and 29 trl some few months ago
- **Banks** supplied RMB 21 trl of the y/y increase – which implied a gradual decline in the percentage growth rate
- **Local governments** have not accelerated their credit uptake as expected (or rather assumed by the authorities). Last summer, the central authorities 'ordered' local governments to increase lending, and they did, but just in one month, before reducing issuances again
- Growth in other credit – via the '**shadow credit market' x local gov bonds** – at 0.5 trl is well below the 6 trl growth in 2020 (a dramatic slowdown, like many times before)

Big picture: Credit growth is slowing

… even if central authorities have ordered local governments to borrow more

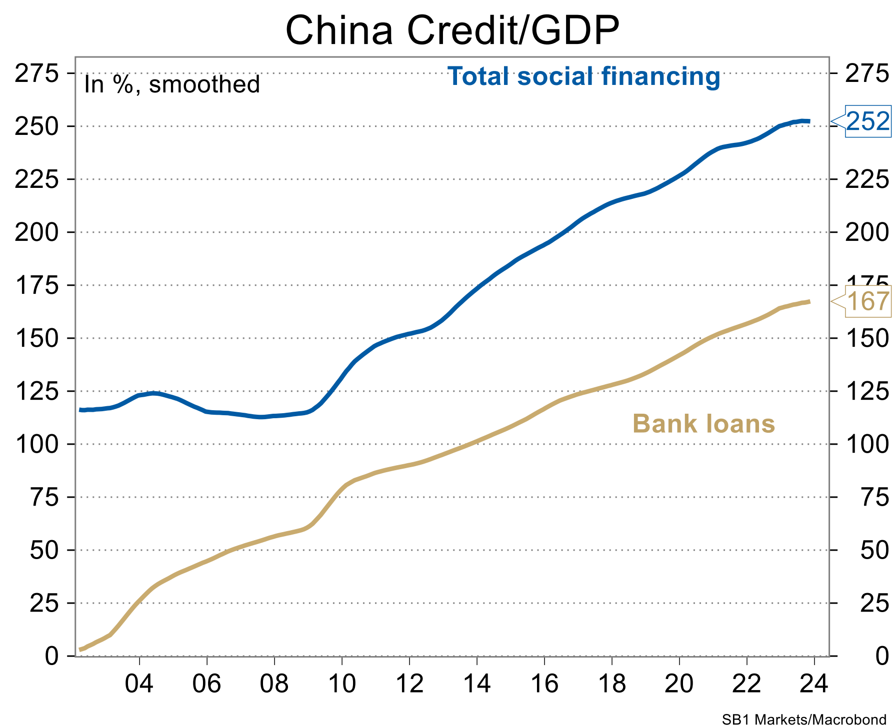


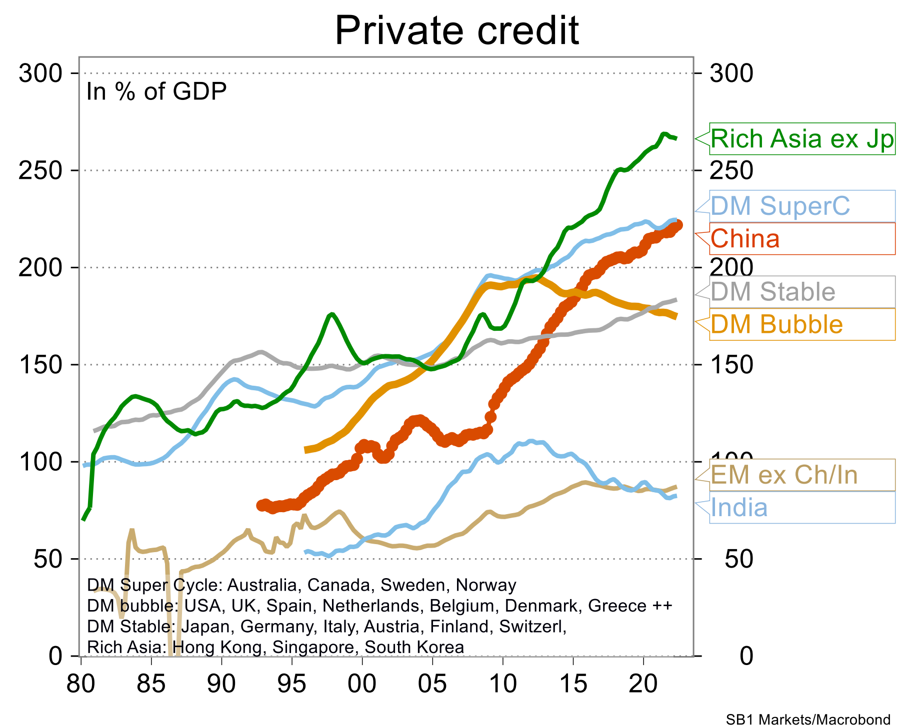


- **The credit impulse** (<u>change</u> in credit growth vs. nominal GDP) has turned negative again, after been marginally positive some few months
- The authorities do not want a full blown credit boom – as the debt level is worryingly high – but they need some stimulus now, especially vs. the financially weakened construction sector

Private sector credit: China is an outlier, along with other rich Asian countries

The ‘global’ private sector debt bubble is really a Chinese bubble (with support South K, Singapore, HK)

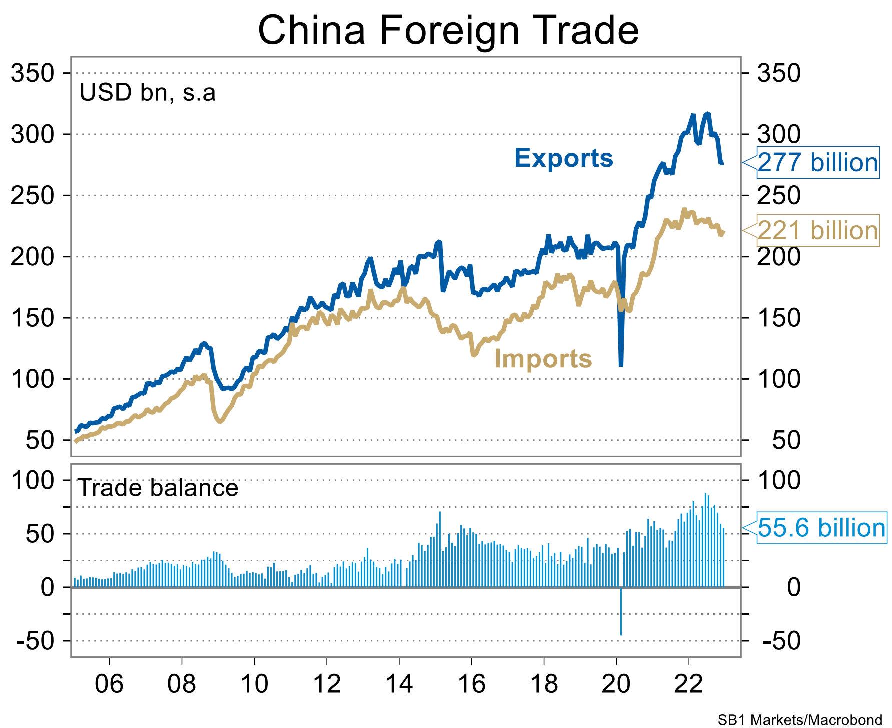


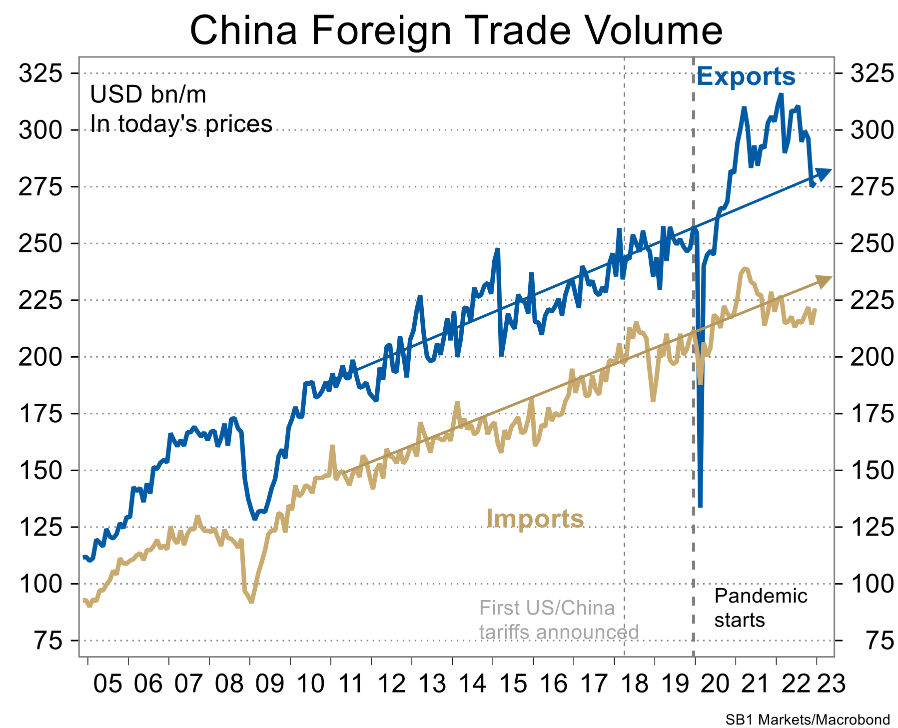


- And there some other outliers as well: DM Supercyclicals (Australia, Canada, Norway, Sweden)

Exports flattened in Dec. Soon we'll get the 'first' real test on foreign demand?

Exports fell sharply in November, probably mostly due to Covid restrictions/lockdowns.

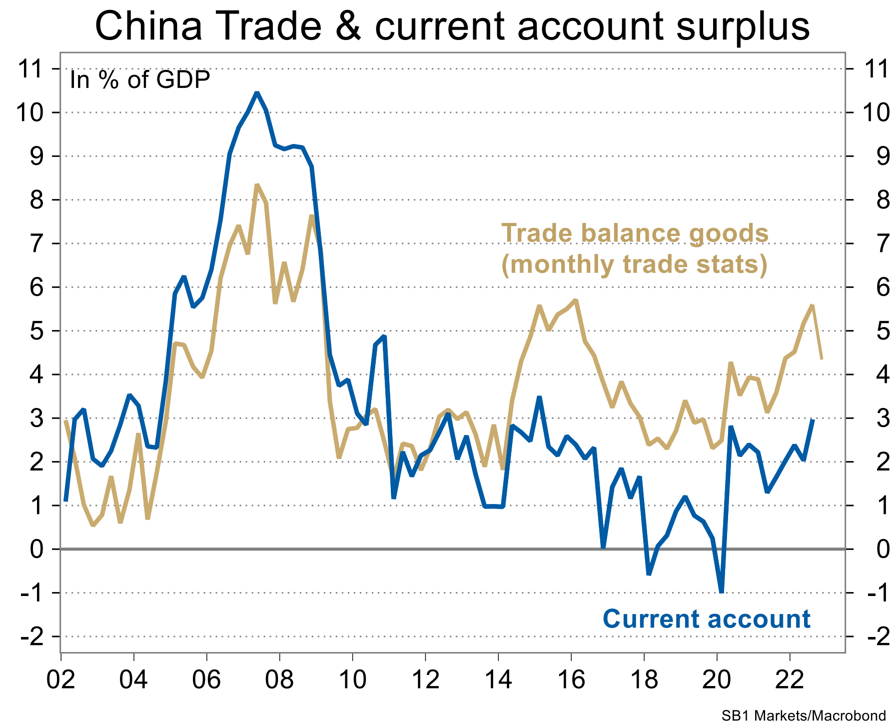


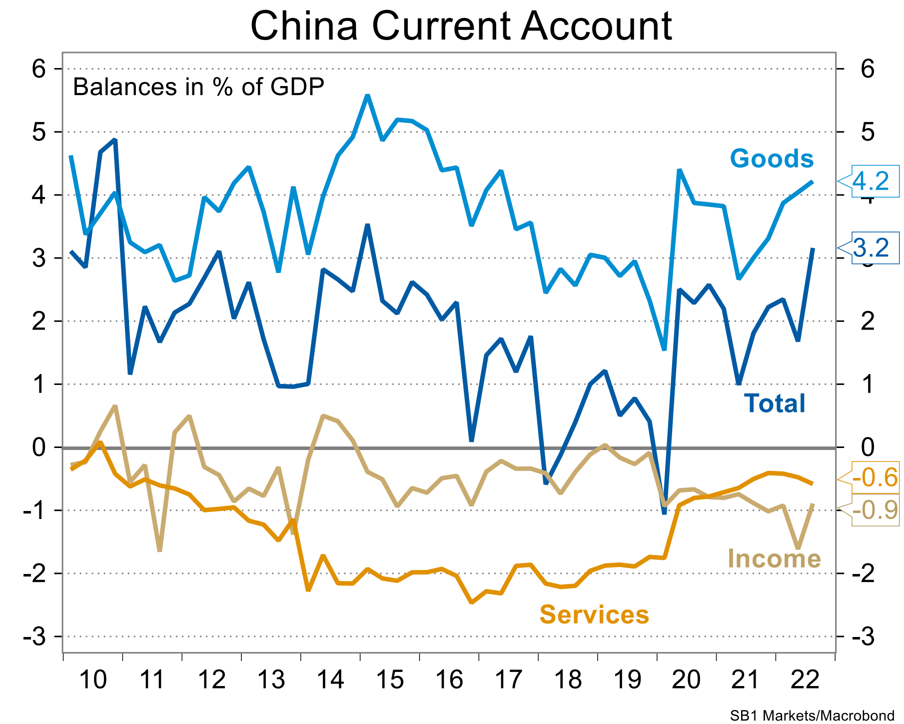


- **Export values were unch. in December** (in USD terms), following the 6% drop in November, to the lowest level since August 2021. Exports are down 10% y/y, 2 pp above expectations. Export values are still up 35% from before the pandemic, and **export volumes** are up 11%, and still not below the pre-pandemic trend (so much for the 'lack of supplies from China story', Chinese exports have been super strong through the pandemic. Exports were no doubt hampered, first by covid restrictions, and from the middle of the month the huge Covid wave and the sharp reduction in mobility. In January, mobility has shot up – and we expect exports for follow suit. However, demand from abroad has also weakened. Trade patterns may turn away from China but the impact will just be very gradual
- **Imports** rose 2% m/m, and are down 7% y/y, 3 pp above expectations. In value terms, imports are heading downwards, but recently not in volume terms. Still, in **volume terms** imports are down by 7% from the peak level last spring – and some 3% below the pre-pandemic trend path (which is not a disaster)
- The **trade surplus** at USD 79 bn, as expected, but 'just' 56 bn seasonally adjusted, and is now trending down

The trade surplus in good fell in Q4, but is trending upwards again

The current account is solid in plus too, as the Chinese have not been travelling abroad for a while. But now…

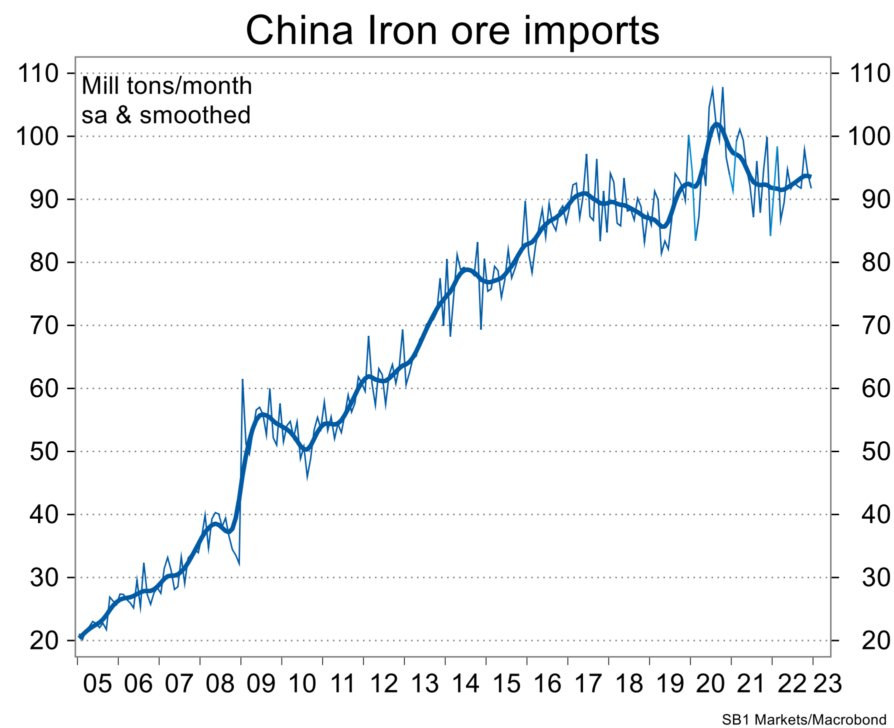




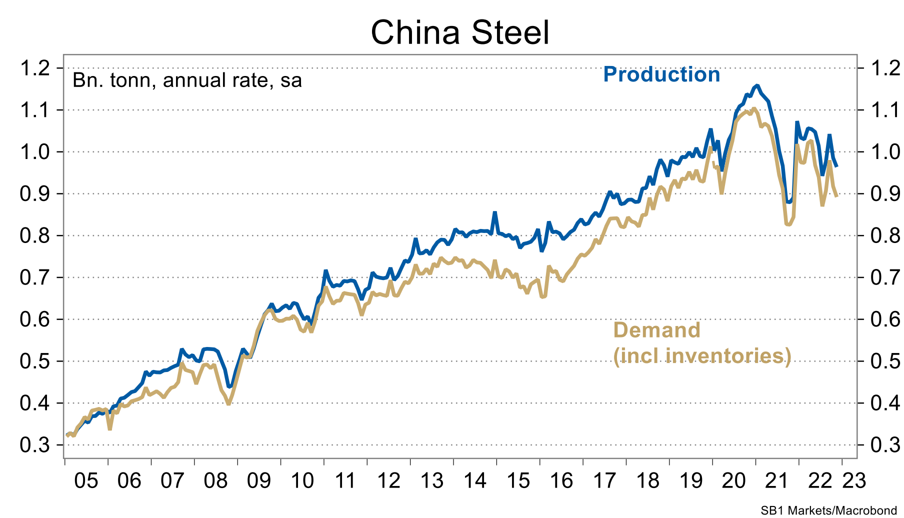
- China runs a deficit in **net (mostly capital) income** from abroad, even if the country has a huge net positive financial position
  - China has invested much in low yielding US government bonds (and other low yielding investments); foreigners have been investing in profitable production capacity in China

Iron ore imports down in Dec, trends slowly up – but is down 10% from peak

Net steel exports stable – equalling 7% of production in rest of the world

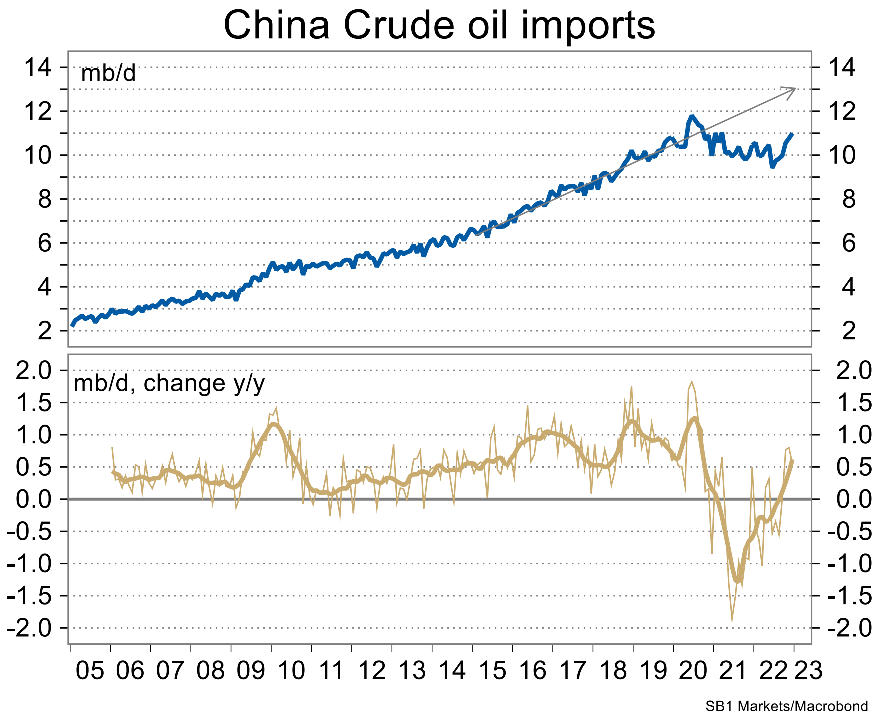


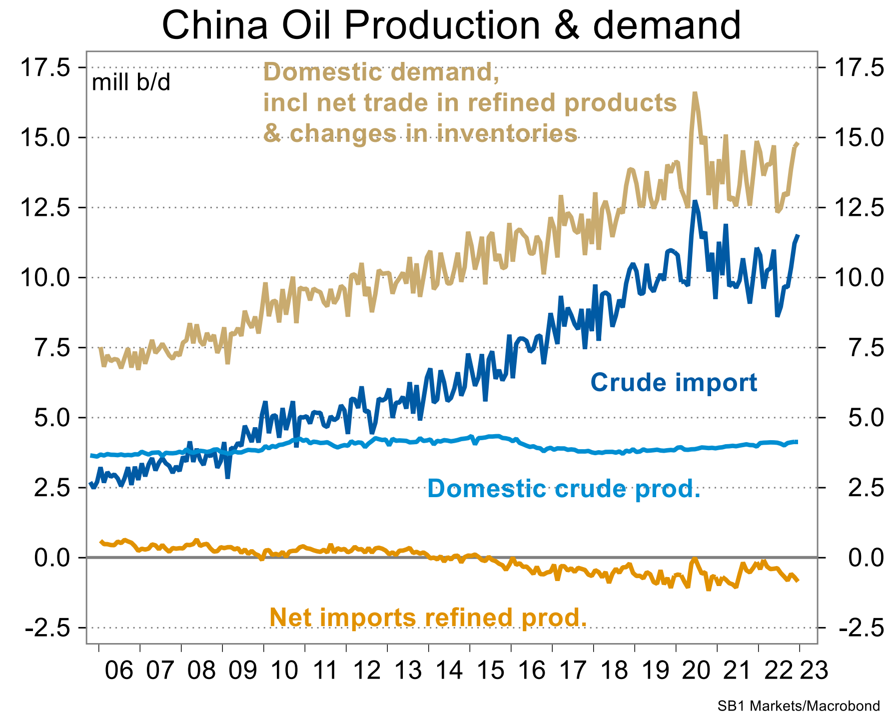
- **Steel production and domestic demand** (incl. inventories) has fallen since early 2021 but not by much vs. the decline in construction starts



Crude oil imports up 1 mb/d recent months, 2 more to go?

China will 'reopen' as the Covid wave most likely is on the retreat. Transport activity has recovered. More oil needed?

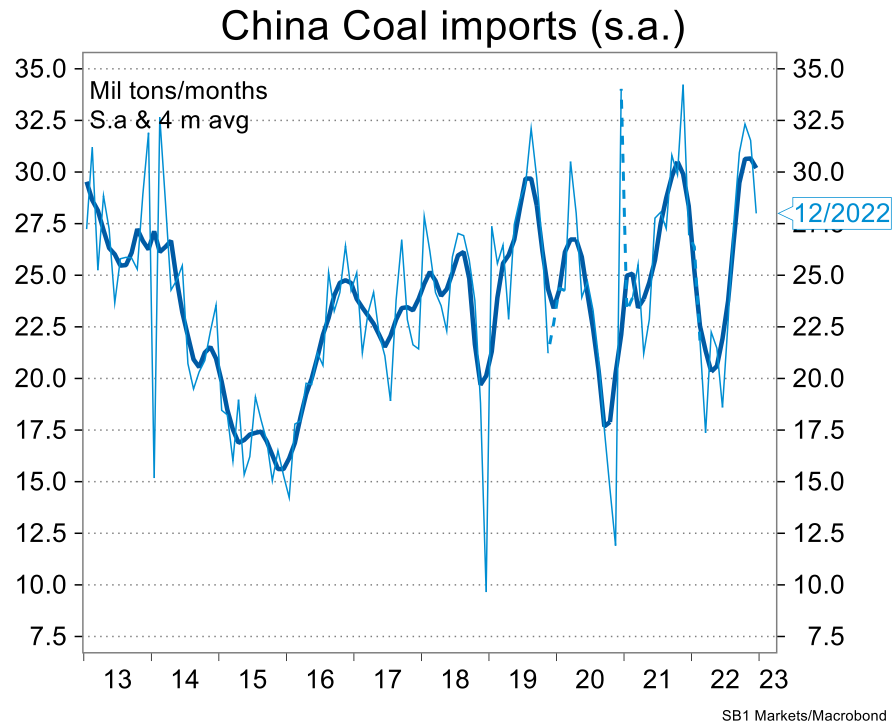


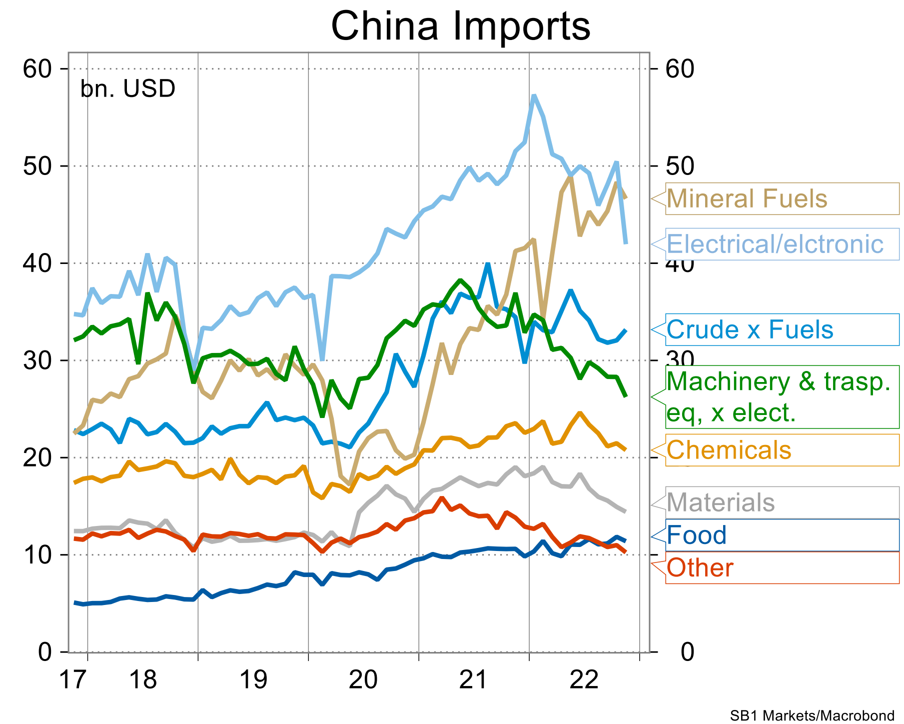


- The pandemic has reduced **road transport** (both persons & probably also goods). In addition, **construction activity** has fallen from early 2021
- **Demand for oil** will very likely increase as the society and the economy is now returning to more normal ways of life. **Road traffic** has recovered rapidly recent weeks/day, and airline traffic will very likely follow suit. However, construction activity may harder to get back to normal, keeping diesel demand lower than normal for still a while

Coal imports down in December but remain at high level

Imports of most goods are heading down

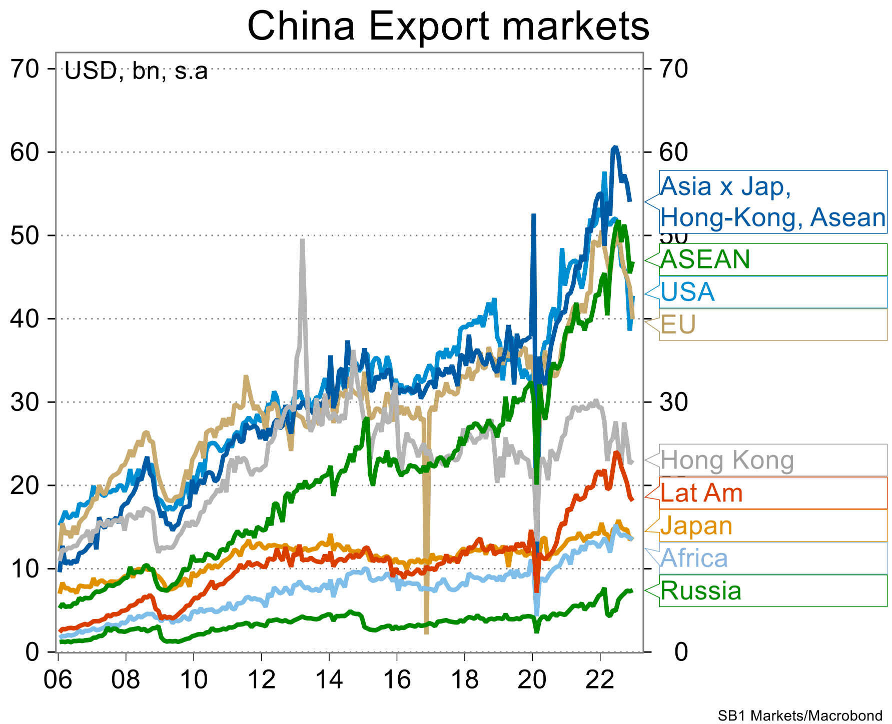


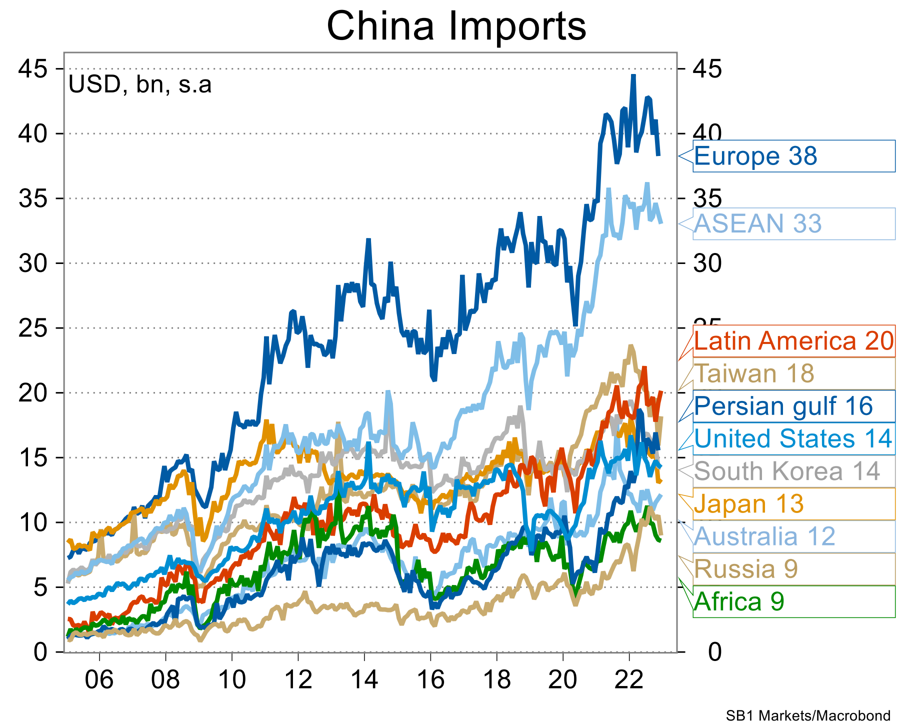


Data for most import sectors are not available for the last month

Exports to the US rose, recovering most of the November crash

Exports to most other markets fell in December – following a significant decline since last summer

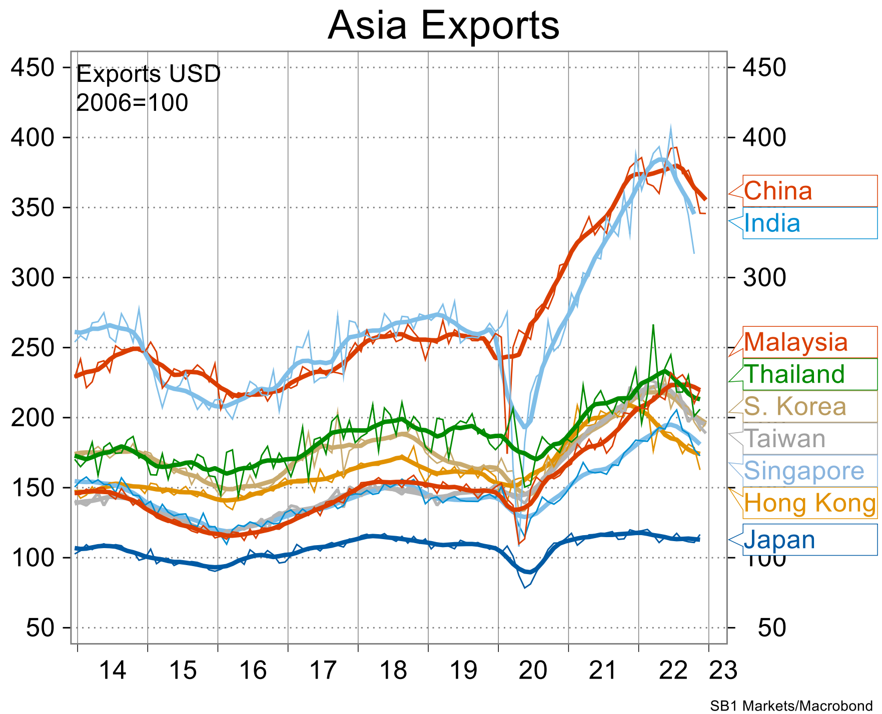


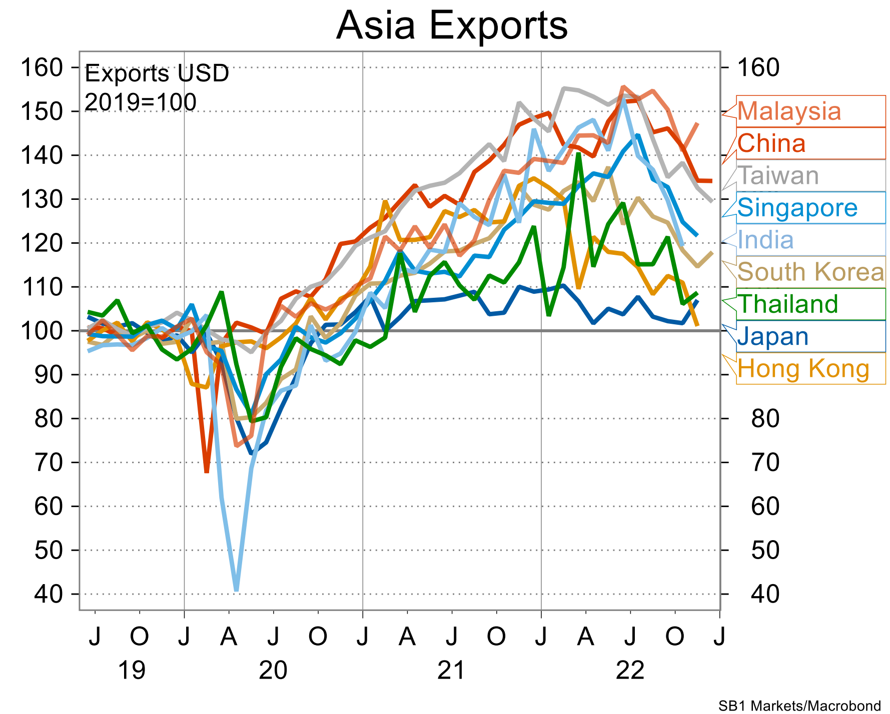


- Exports to the US are down almost 20% from the peak
- Exports to Russia are trending up –and are now back to the pre-war level (and at ATH)

Exports from all other Asian countries on the weak side recent months

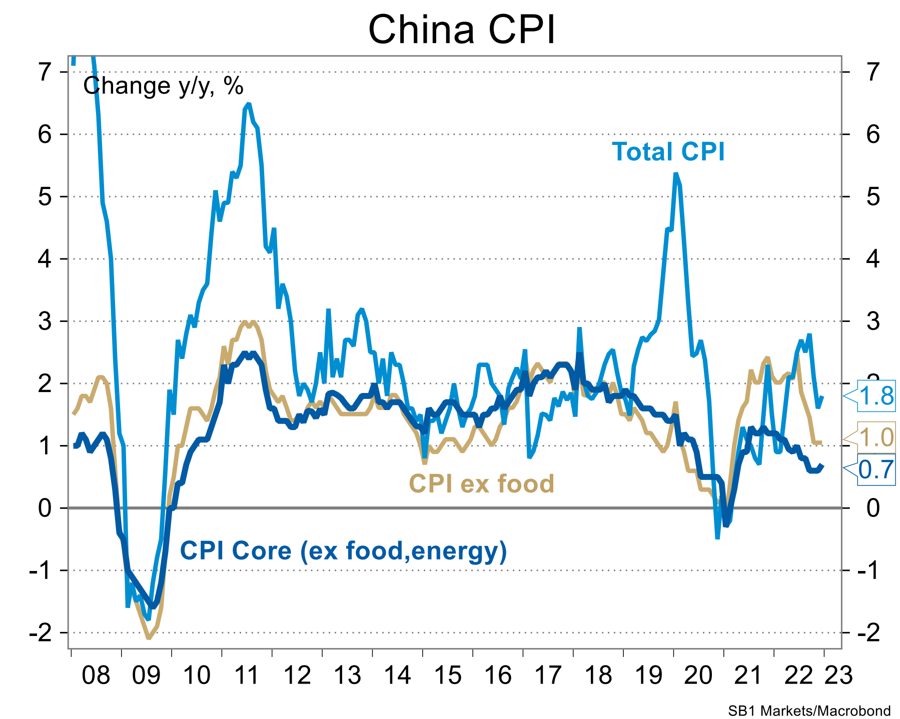
… which confirms the lack of global demand story – not a sudden production problem in Asia

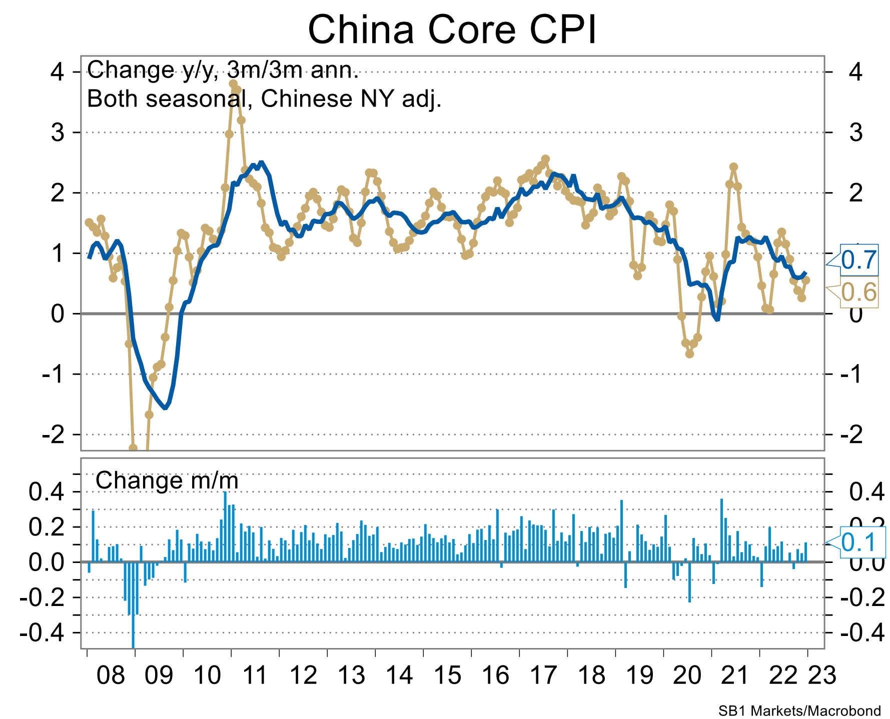




While the west has been struggling with high inflation, China has steered clear

Inflation as expected in December, the core at 0.7%, total at 1.8%

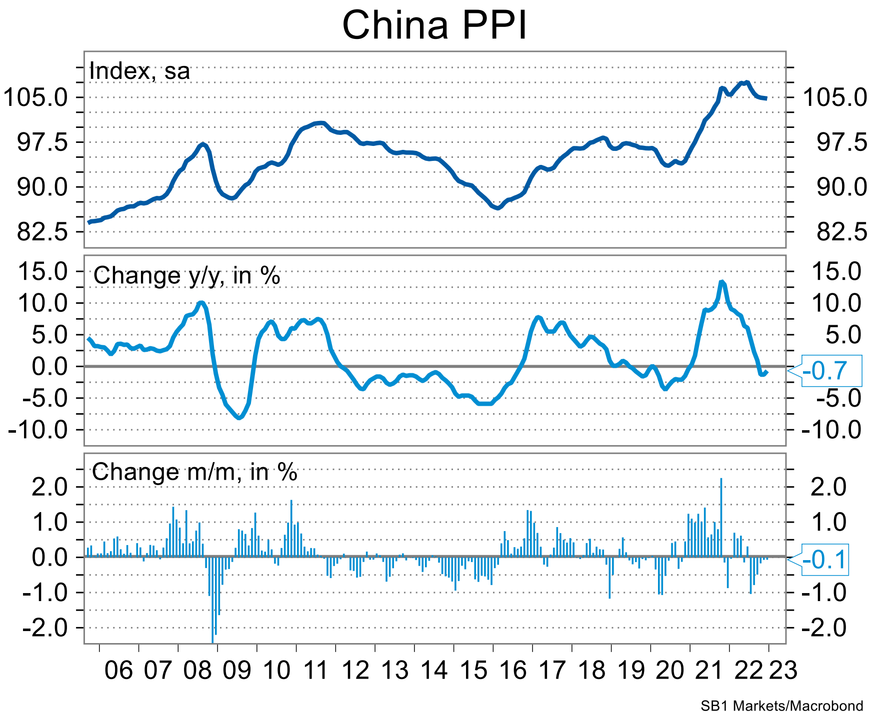


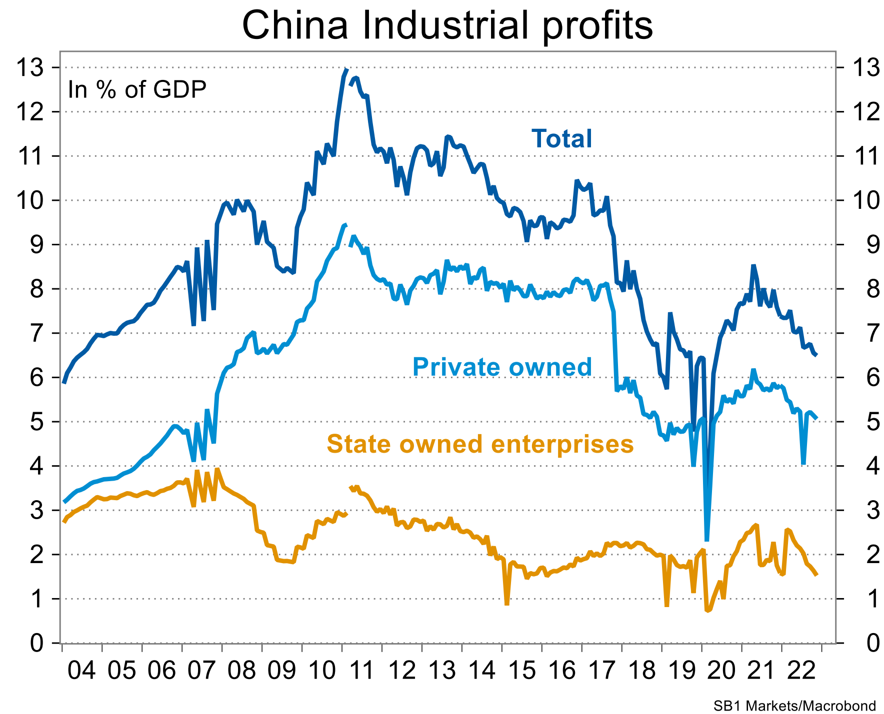


- **Total annual CPI** was up 0.2 pp to 1.8%. Prices were up 0.1% m/m
- **The core CPI** (x energy, food) were up 0.1% m/m, and the annual rate crept up 0.1 p to 0.7% y/y. The 3m/3m rate is at 0.6%
- **Food prices** are up 4.8% y/y, with pork prices in the lead again, up 22% (but down from above 50% in Nov)
- **Gasoline/fuel prices** are up 12% (down from 19% y/y in Sept)
- **Both core & headline inflation** are still low. **Monetary policy** will not respond to actual inflation data if inflation is not really high or low, the real economy and the credit market are more important. Now authorities are trying to kickstart the economy again after the lockdowns

Producer prices keep falling and are down 0.3% y/y

A sign of slowdown in goods inflation globally? Corporate profits are trending down

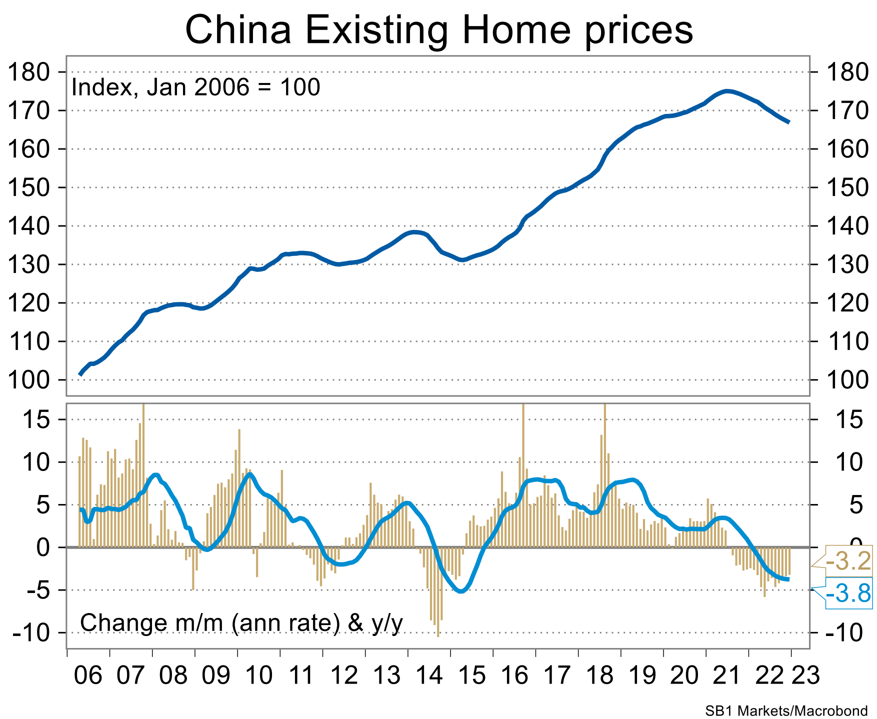


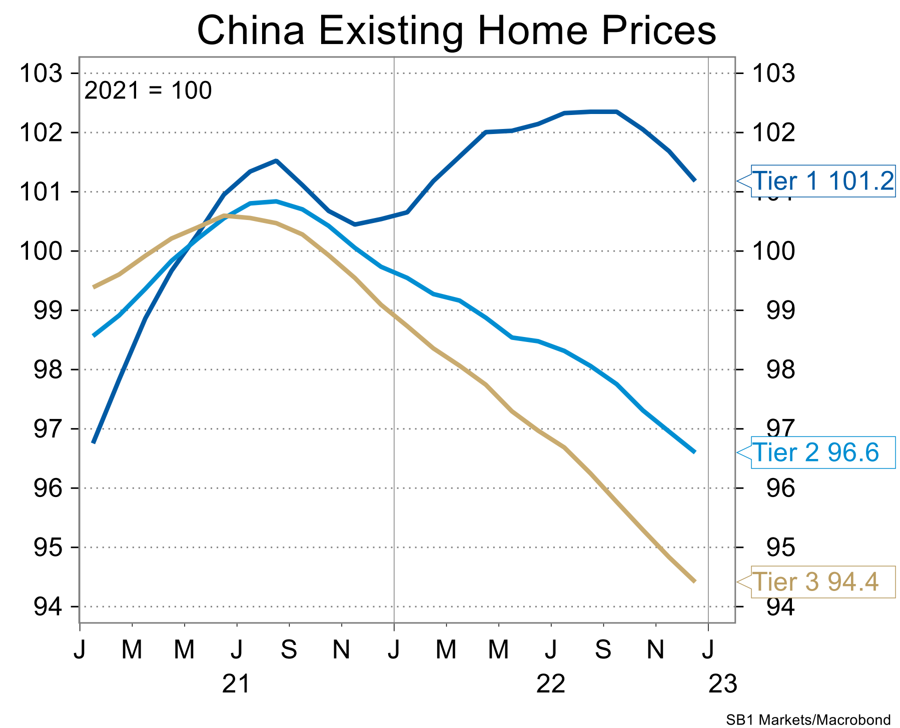


- **At the peak**, the PPI was up 13.5% (last October)
- **The PPI** fell by 0.1% m/m in Dec and has fallen the past 5 months. Global demand is no doubt softening
- **Consumer goods** are up just 1.8% y/y, durable consumer goods are up 0.6%, while raw materials are up 1.2% - down from 26% a year ago
- The correlation between PPI and CPI in China is not impressive (but far better with the US CPI)
- **Profits in privately owned industrial enterprises** are declining in % of GDP, as are profits in state owned companies

Existing home prices fell further in November – for the 17th month in a row

- the longest stretch with falling prices ever – and they are falling everywhere. New home prices on the way down too

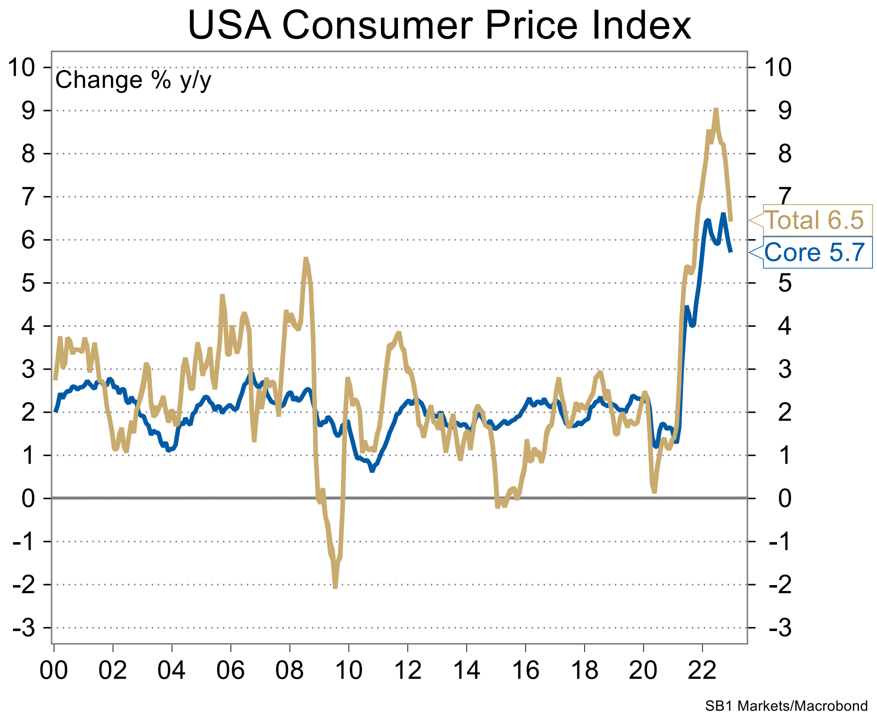


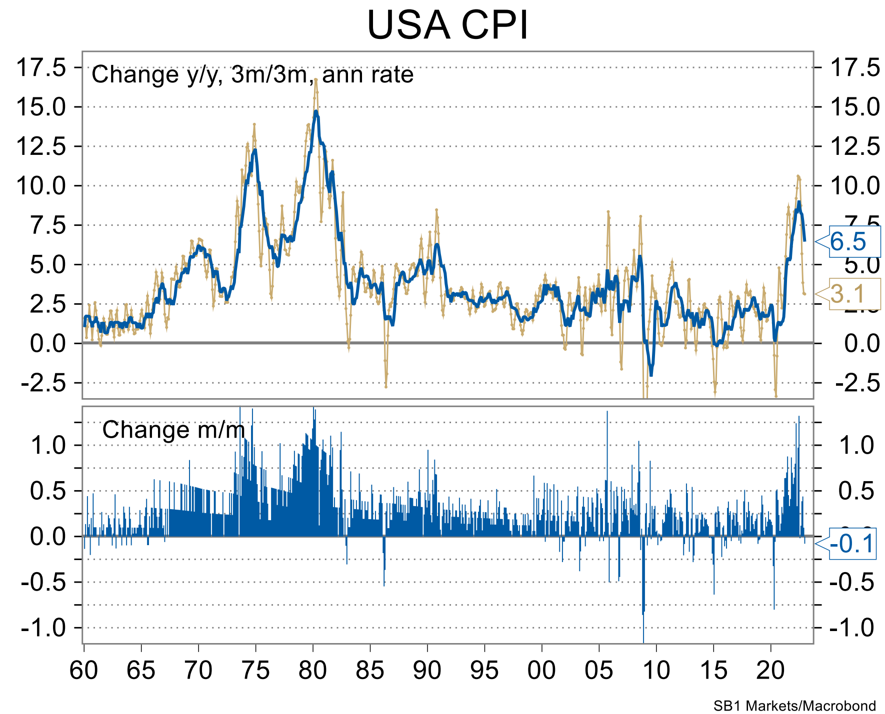


- **Existing home prices** peaked in July-21, and have been falling at a gradually faster pace, until May, where prices fell at a 5.8% annualised pace. In December, prices fell at 3.2% pace. Prices are down 3.8% y/y, less than the price setback in 2014/15. However, the current setback has now lasted longer than the previous.
- Prices are falling in the four largest Tier 1 cities for the 3rd month in a row , but prices are falling at the fastest pace in the 'smaller' Tier 3 cities
- **New home prices** have been falling since Sep-21 but at a slower pace than existing home prices, and in Dec new home prices fell at just a 1% annualised pace m/m , and are down 2.3% y/y
- **Central authorities** have signalled willingness to expand credit supply again, both to finance infrastructure projects and the construction sector, as well as providing support to home buyers. So far without any impact. However, more measures recently – and they may work

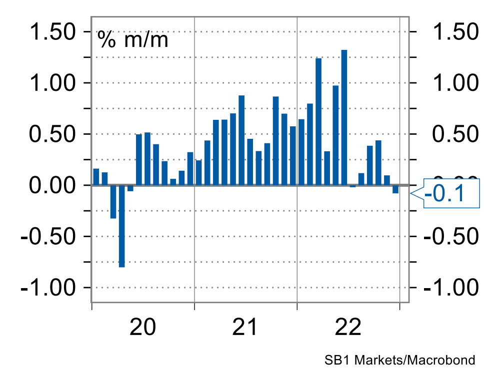
CPI has peaked. More to come

CPI fell 0.1%, as expected and the annual rate fell to 6.5% from 7.1%



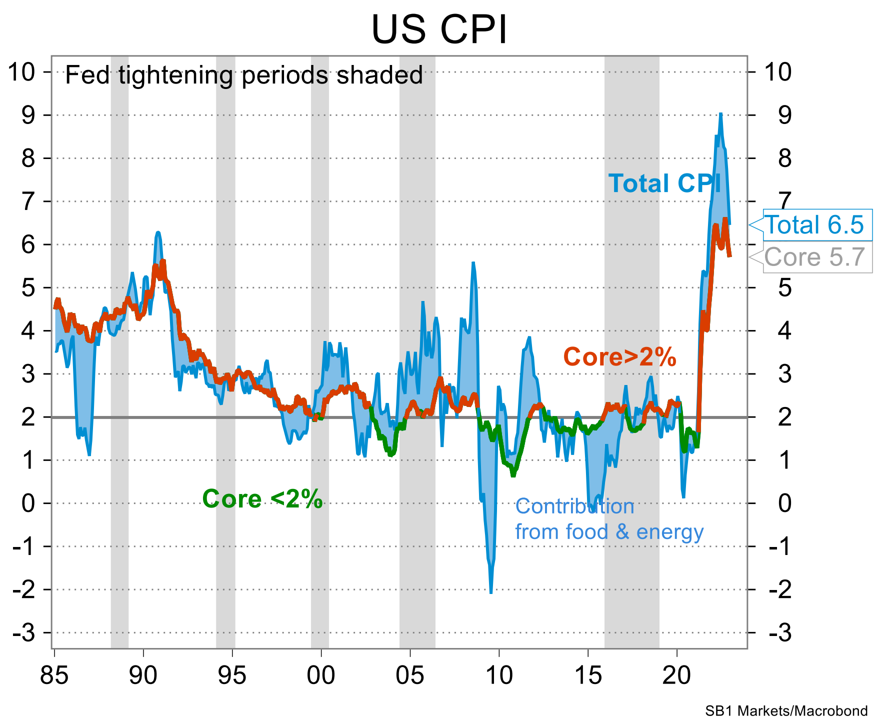


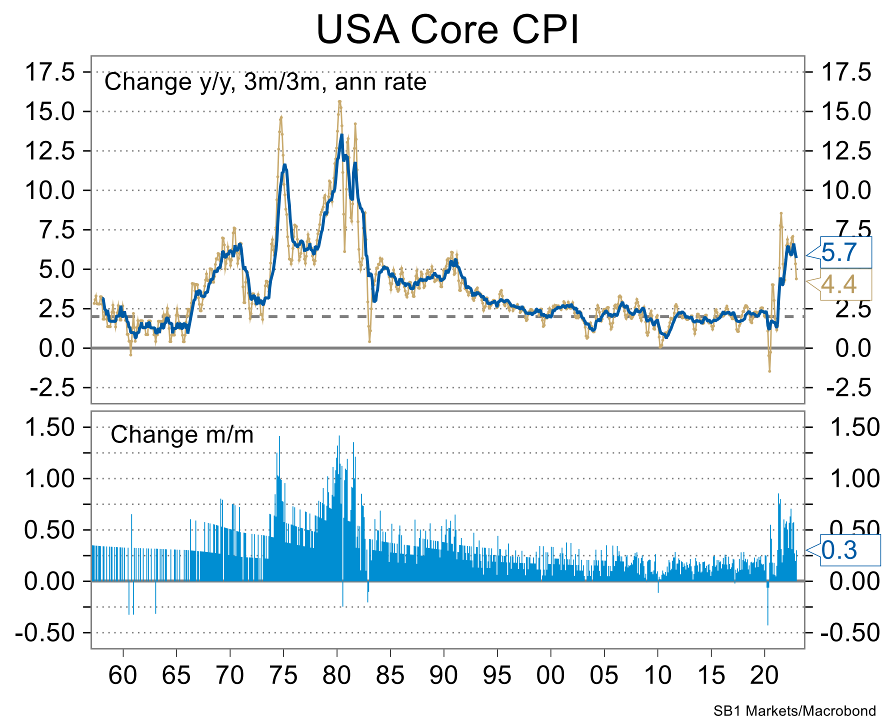
- **Headline CPI** fell 0.1%, the first monthly decline since spring 2020, when prices fell sharply. The annual rate slowed 0.6 pp to 6.5% in December, as expected, the 6th monthly decline in row. The 3m/3m rate fell to 3.1% - from above 10% some few months ago
- **Surveys** report a rapid slowdown in price increases, especially ISM markets, and the NFIB survey (check here)
- **Markets** rallied, for good reasons. Inflation is definitely on the way down. Now, the decline in driven by lower corporate margins, and that's just a temporary relief. Wage inflation remains Fed's main concern, but even here news have been on the positive side recently, and last week the Atlanta Fed median wage tracker slowed somewhat – but all wage indicators still report wage inflation well above a level that will yield 2% CPI inflation

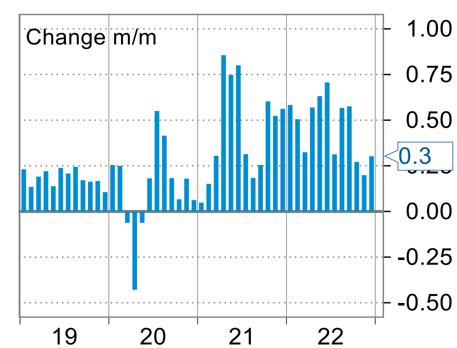


Core prices up 0.3% m/m, as expected, and down 0.3 pp to 5.7% y/y

The 3m/3m rate at 4.4% confirms that underlying inflation has peaked but remains too high

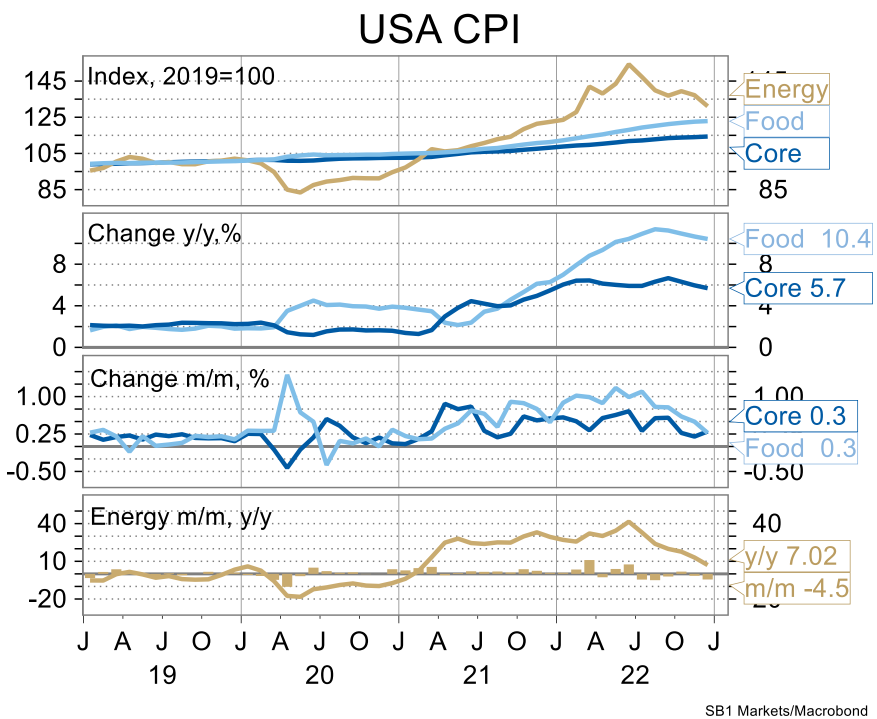


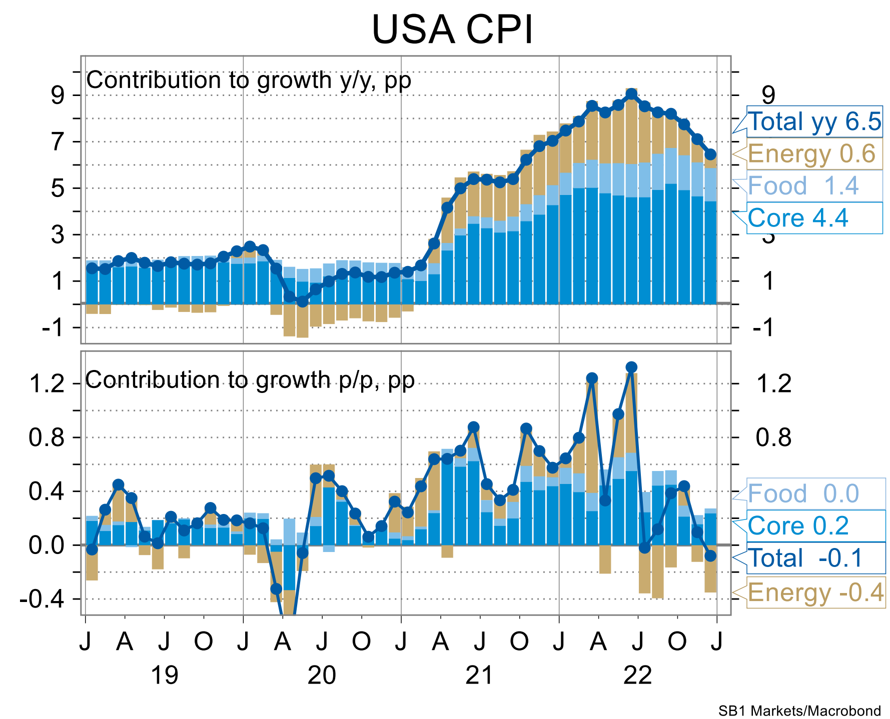




Energy prices are falling, food price inflation is slowing – as is core inflation

Energy prices will soon turn negative y/y. Food prices are much higher than food commodity prices suggest

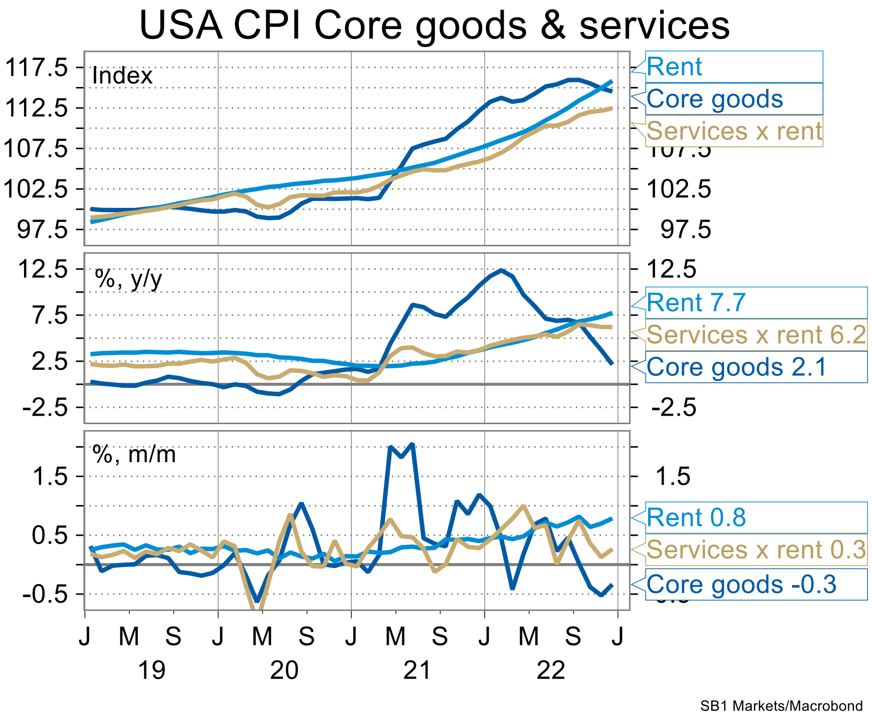


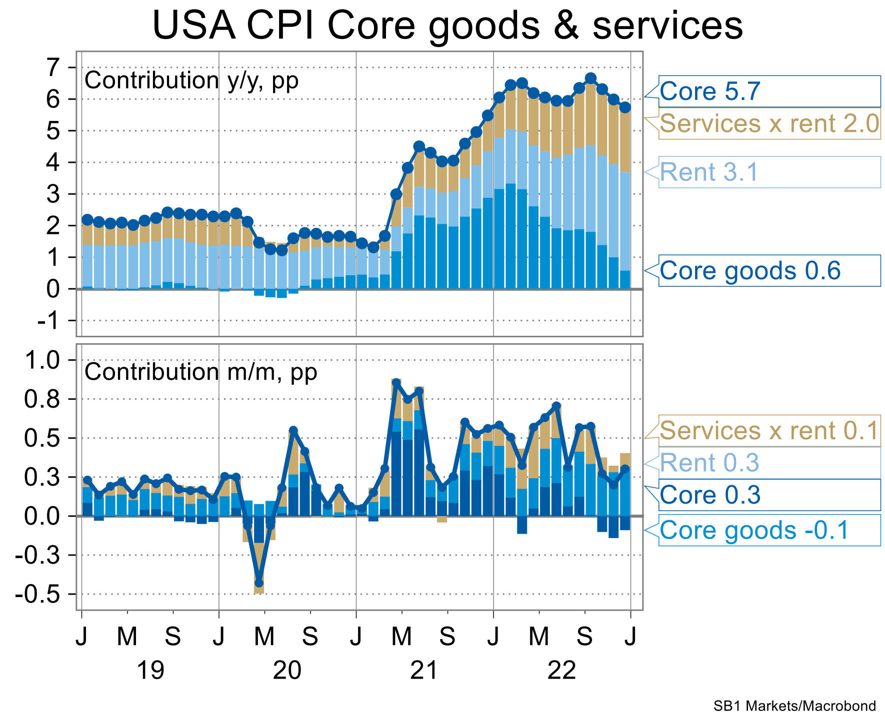


- **The headline CPI** fell 0.1% in December, as expected. The annual rate fell to 6.5% from 7.1%, also as expected. The trend is down both for monthly and annual growth rates
- **Energy** prices fell 4.5% m/m, and will very likely decline further in January. Prices are still up 7% y/y, contributing 0.6 pp to growth in annual headliner CPI
- **Food** price inflation is slowing but prices rose another 0.3% in December – but monthly growth is slowing rapidly. Prices are up 10.4% y/y, contributing 1.4%
- **Core inflation** has clearly peaked too, as goods prices are now declining (more next page)

Core goods prices are falling – services inflation slowing. But rents…

Core goods prices fell 0.3% m/m in December, and are up just 2.1% y/y, from 12.5% at the peak in early 2022



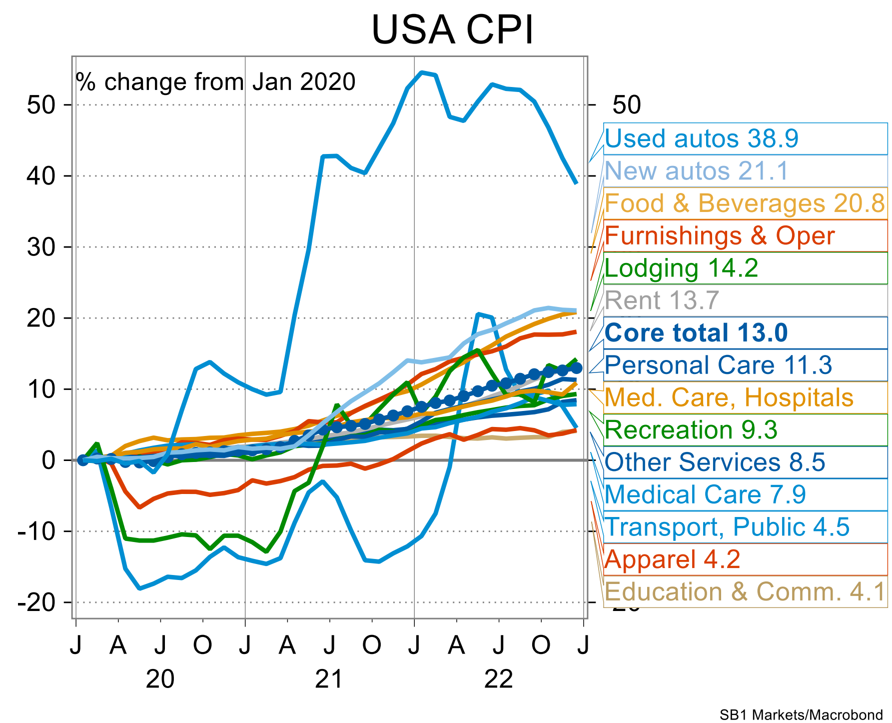


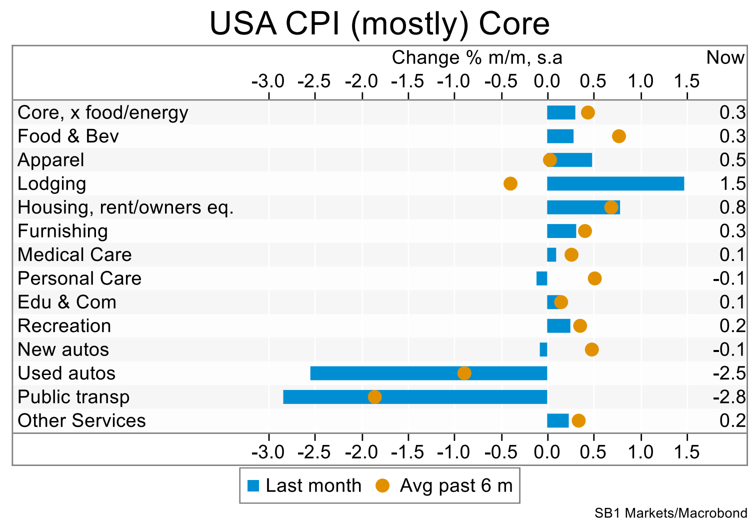
- A further normalisation of **goods prices** is likely, as demand slows, raw material prices are coming down, alongside transportation costs – and as signalled by the PPI
- **Rent inflation** is still on the way up – up 0.8% m/m and by 7.7% y/y! Rents on new leases very likely are moderating, the rent index in the CPI should follow suit after some months
- However, as Powell has stressed several times, also at last week's press conference, inflation will not come down to a sustainable level before **service sector inflation** (ex residential rents) also yields. Monthly changes have slowed somewhat recent months, and the annual rate has probably peaked, but remains at 6.2%, unchanged from November
- *More details on the following pages*

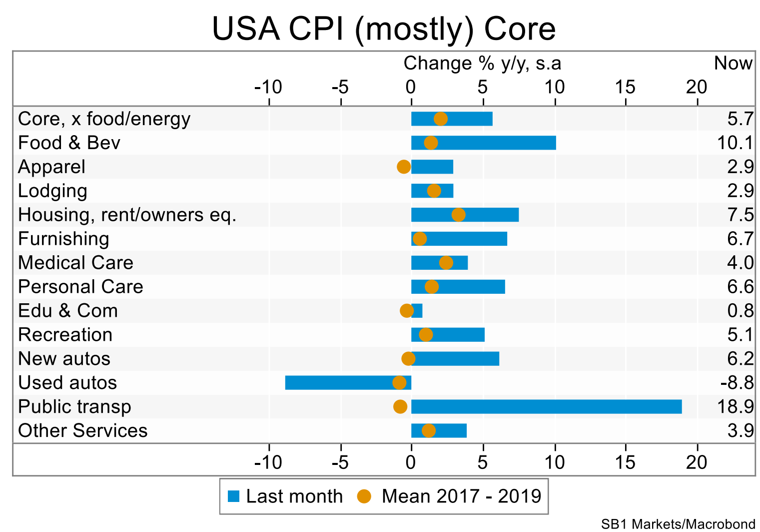
In the core CPI: Rent 40%,

Used autos & airfares cheaper in December, most other prices rose

Used auto prices are falling rapidly – and new auto prices have flattened recent months





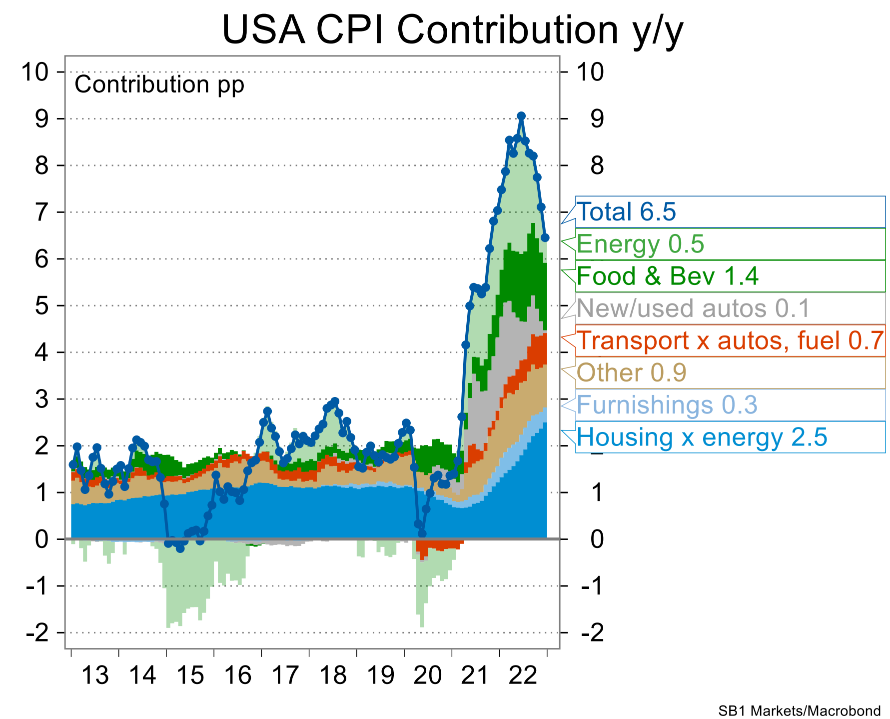


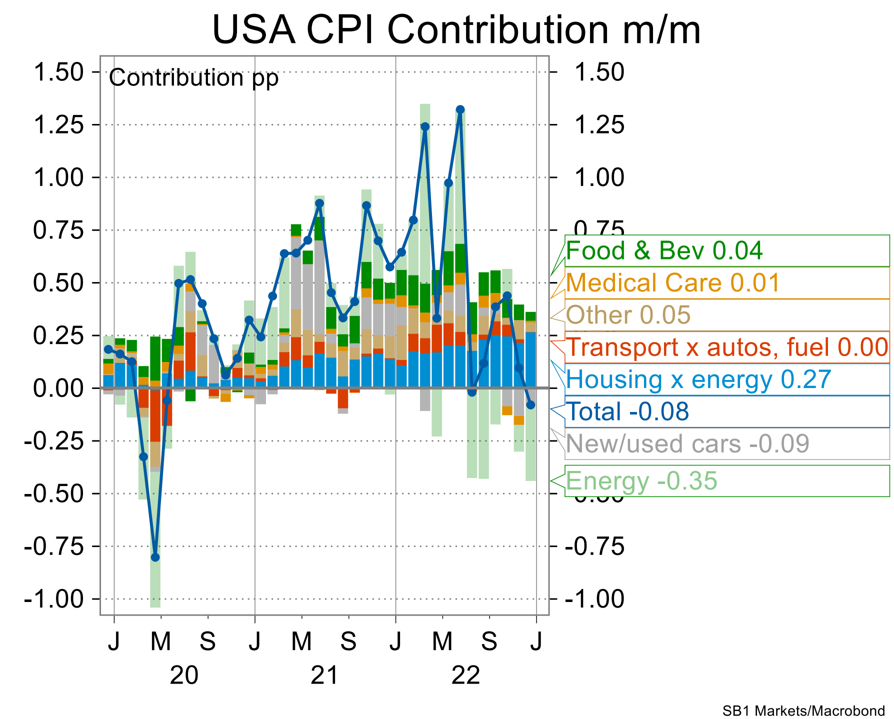
- **Rents** are up 7.5% y/y, lifting the CPI by 2.5%, alone!
- One day: A huge downside to **used auto prices** – and hopefully for some others as well, like food and furnishing prices

SpareBank 1 MARKETS

Energy & transport (incl. autos) explain (just) 1.3 pp of the 6.5% lift in total CPI

The rest is still up at a rapid pace



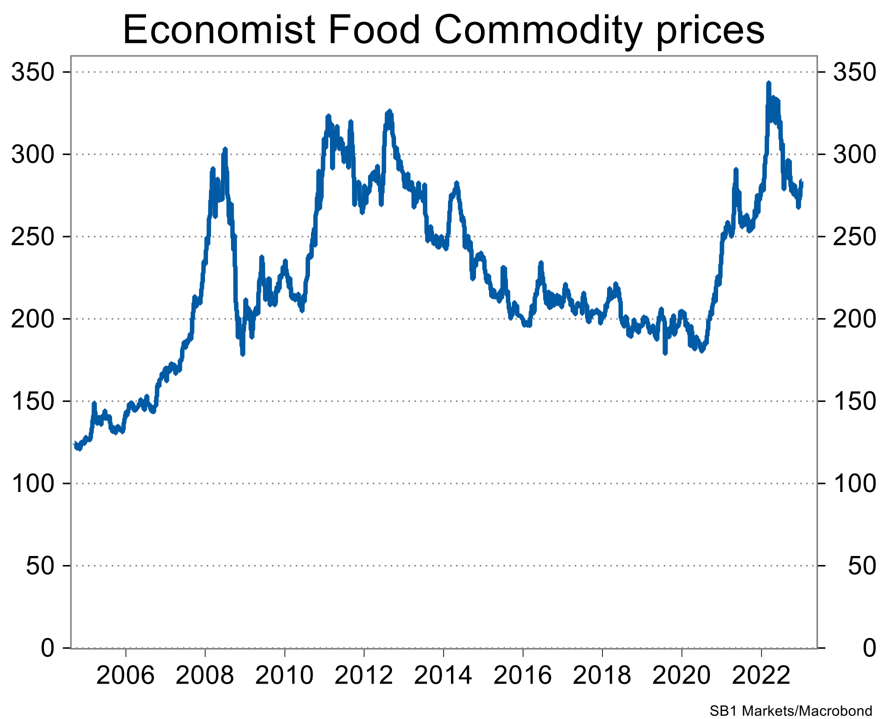


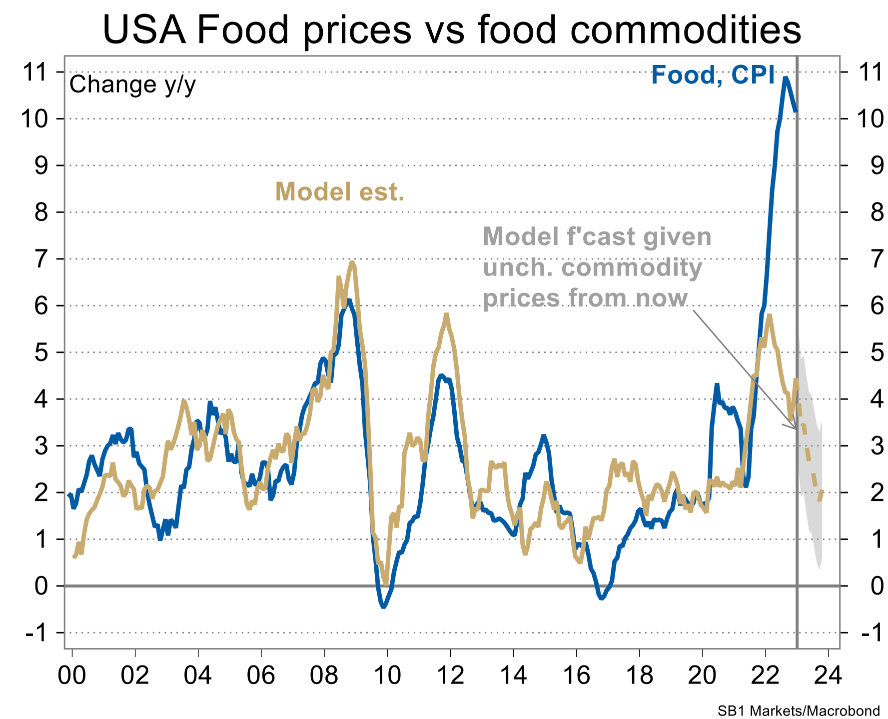
- **Energy** prices fell further in December but are still sharply up y/y
- **However, excluding** the 2 pp contribution to the headline CPI from energy & transport, **"remaining" inflation** has flattened
- **Housing x energy** (and x lodging) is contributing by 2.4 pp. Rents as measured in the CPI are up 7.1% y/y, but the upside is probably now limited

Lodging away from home (incl hotels) is not included in housing in the charts above

Food prices will have to come down??

They are much higher than what can be explained by food commodity prices

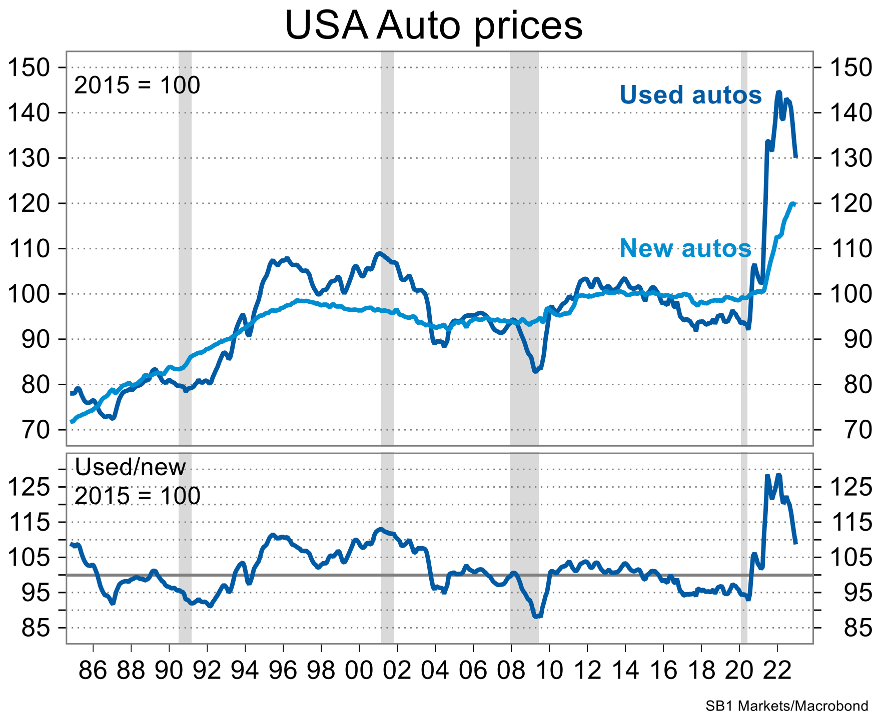




- Why have food prices at the retail level exploded vs. food commodities? The candidates: Freight costs, processing costs, distribution costs, (including energy and wages at each element in the value chain) – and the retail trade sector has increased its profit margins (according to national accounts). Are these factors permanent? We very much doubt it
- If we are right, food inflation will come down sharply

Used auto prices are finally yielding but are still too high

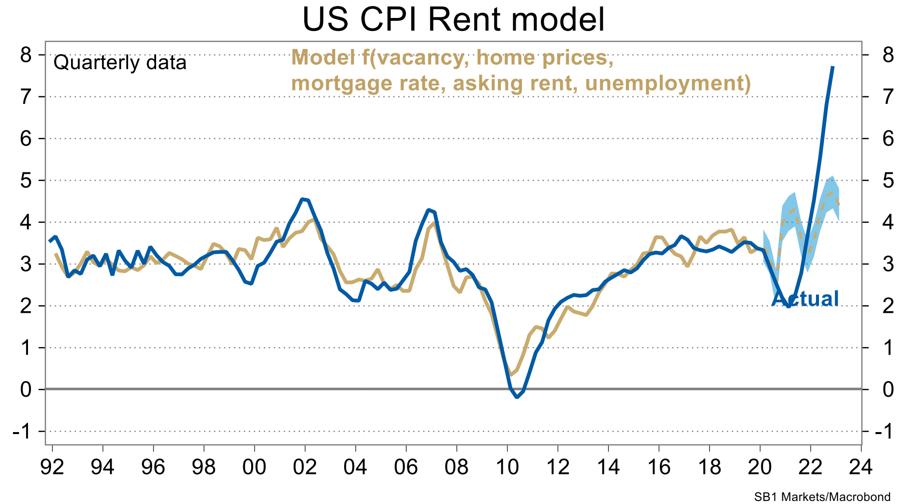
New auto prices are still soaring – but for how long?



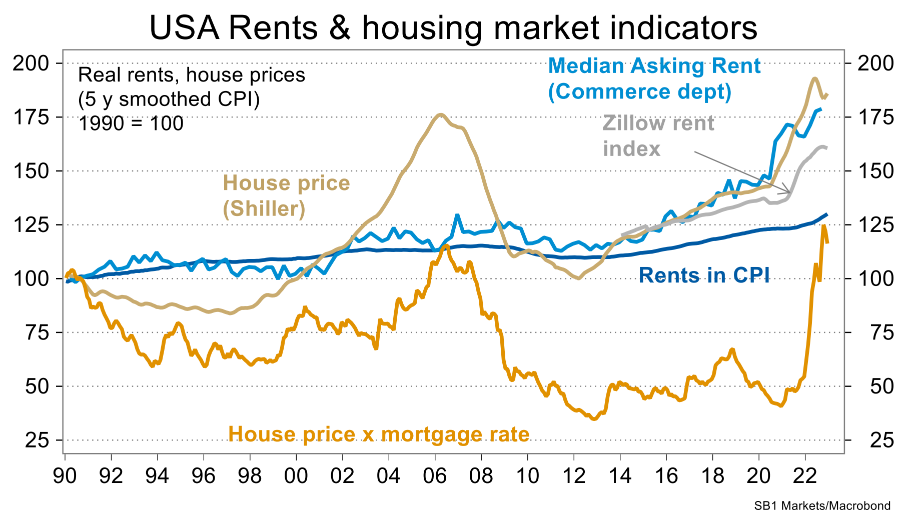
- At one stage, at least **used auto prices** will come down to a normal level vs. new car prices
- **New auto prices** have shot up sharply recent months – and these prices will also very likely return to a more normal level – production costs are not up 26% through the pandemic!
  - We have so far assumed that demand for autos was higher than production capacity but there are reports of higher inventories of new cars

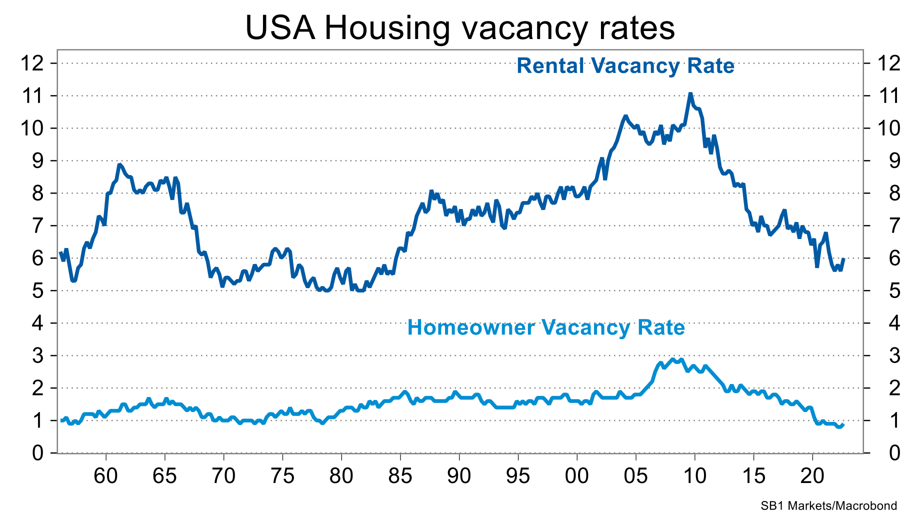
Rent inflation should one day slow down, as market rents are flattening

Rents are up 7.7% y/y, while signals from the rental market are mixed



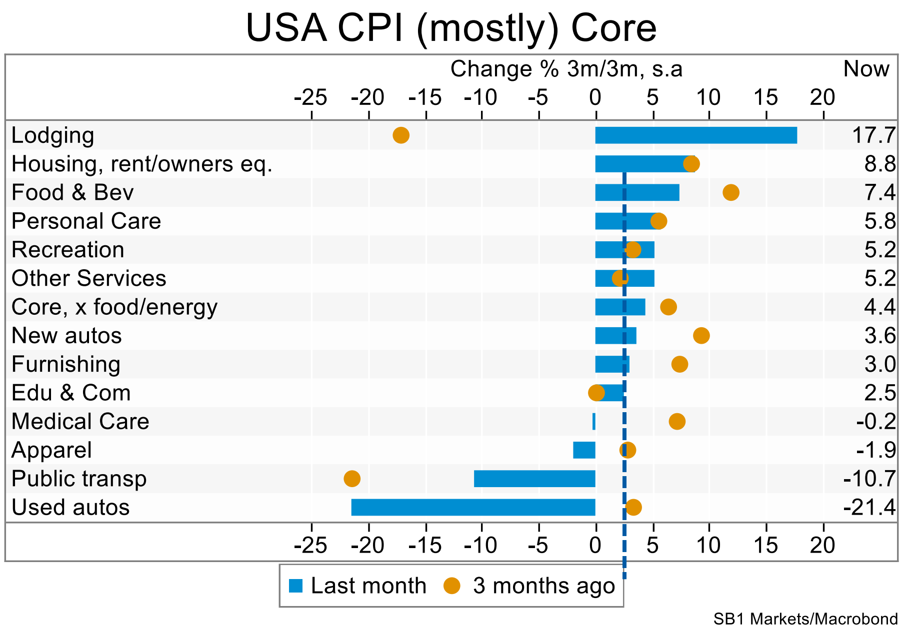
- **The official (Commerce dept) median rental asking price** has fallen somewhat recent months, and other surveys signal slowing rents (but not declining rents), house prices are turning south – but it typically takes time before rents in the CPI follow suit
- **The rental vacancy rate** has fallen sharply recent quarters. The **homeowner homes' vacancy rate** is still trending down, and is also at an ATL. Alas, a tight housing rental market
- **Rent inflation measured in the CPI** has accelerated to 7.7% and total housing costs (ex energy) contribute 2.5 pp to annual headline inflation!
- **Our model**, when assuming a substantial slowdown in rental asking price inflation and a rapid decline in existing house price inflation the coming quarters, and a decline in the 30 y mortgage rate to 6%, signals a much lower rent inflation than the current rate

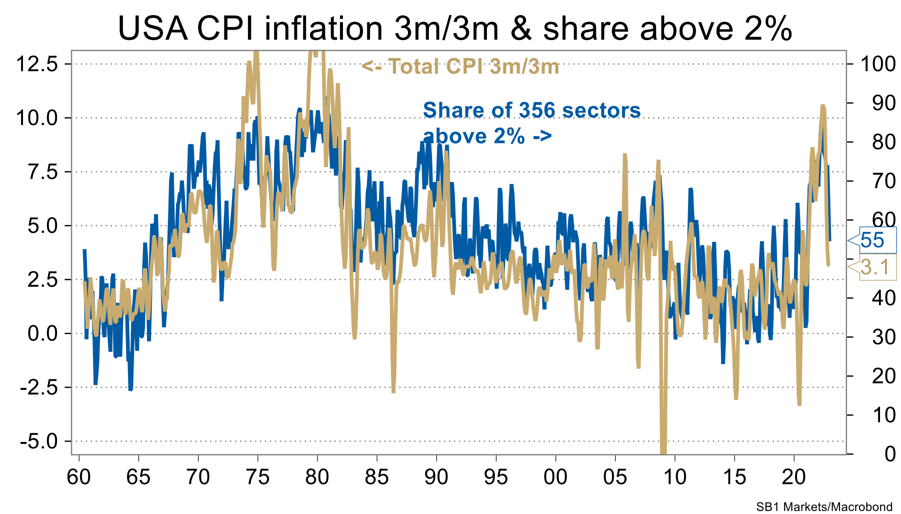


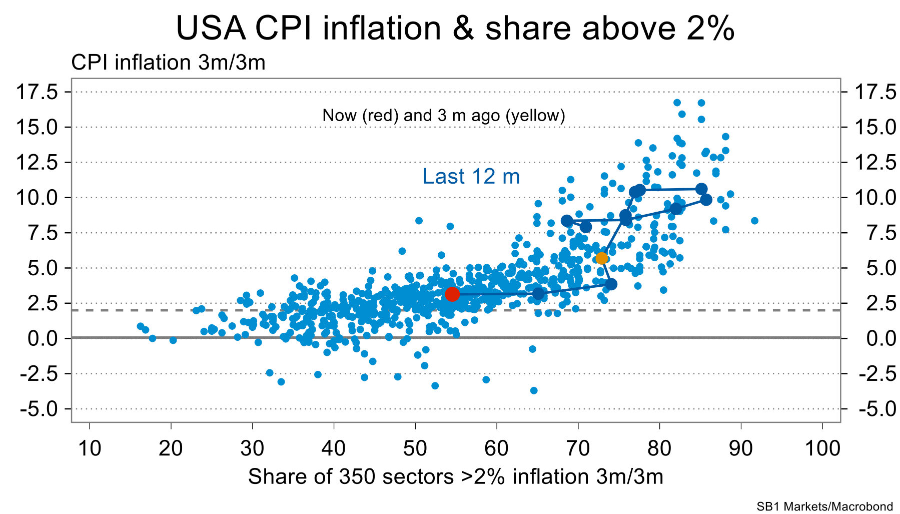


Inflation measured 3m/3m: More contributors on the downside

In addition, prices are up ‘just’ 3.1% 3m/3m, down from above 10% at the peak



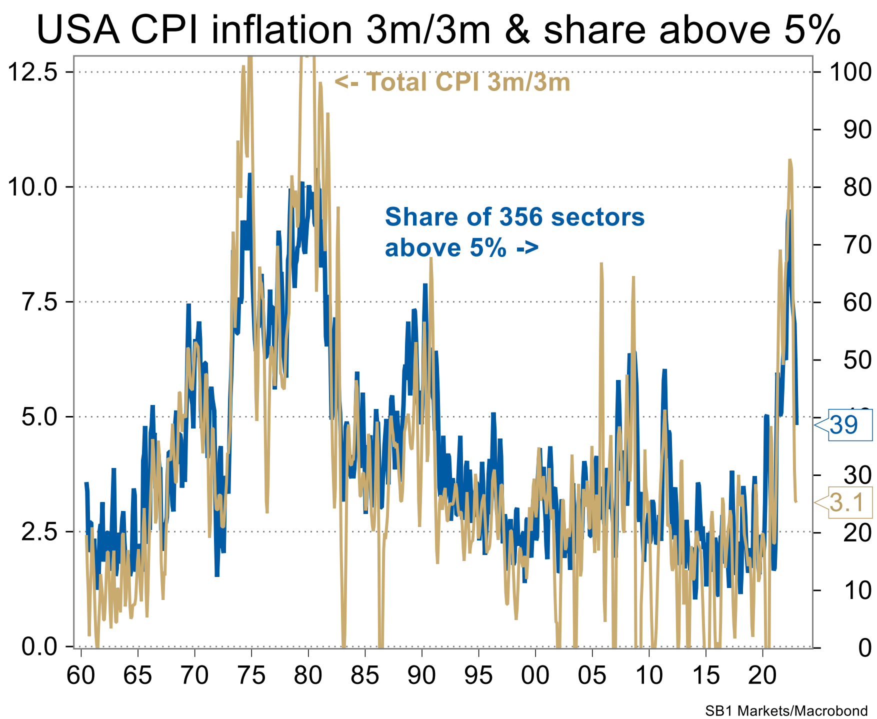


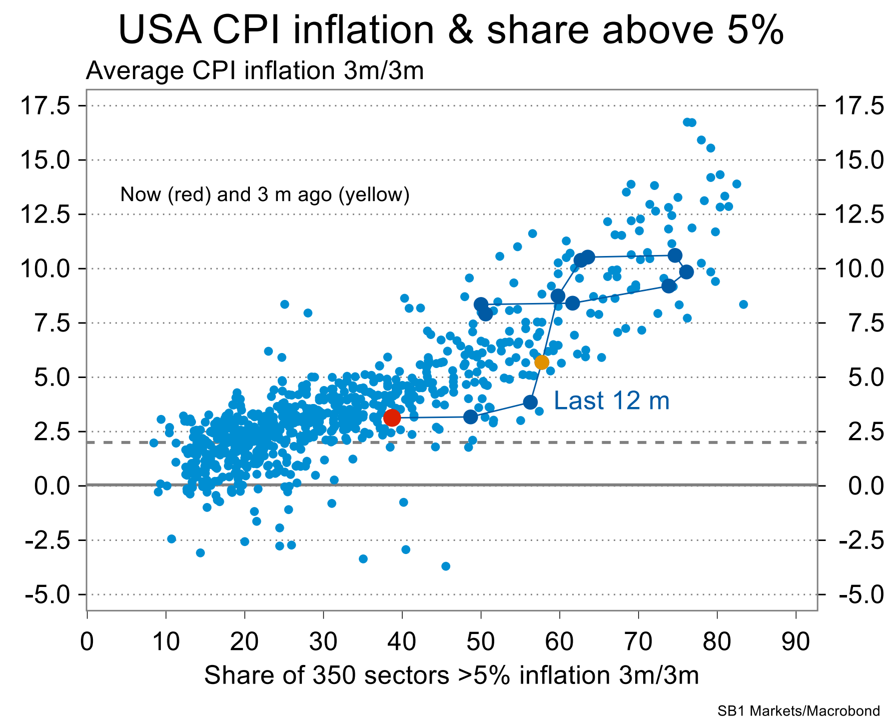


- ‘Just’ 55% of the CPI items are up more than 2% 3m/3m, down from 65% last month and almost 90% at the peak
- A substantial negative drag from lodging and public transport recent months will surely not last but a large majority of the main sectors report now lower underlying price growth

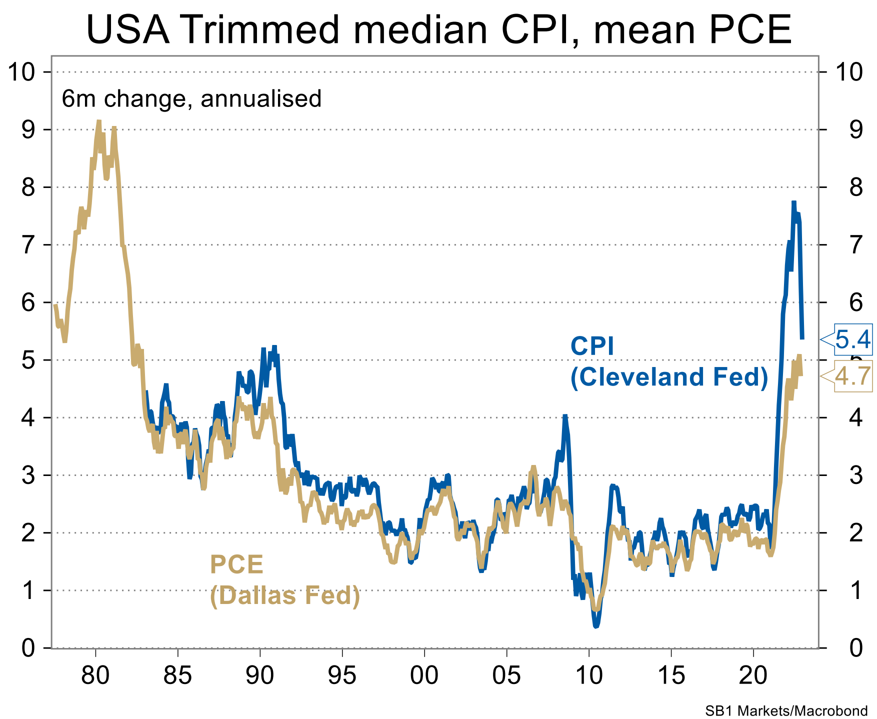
‘Just’ 39% of sub-indices are up more than 5% 3m/3m

‘Just’ because the share has fallen from almost 80% (and 49% last month)





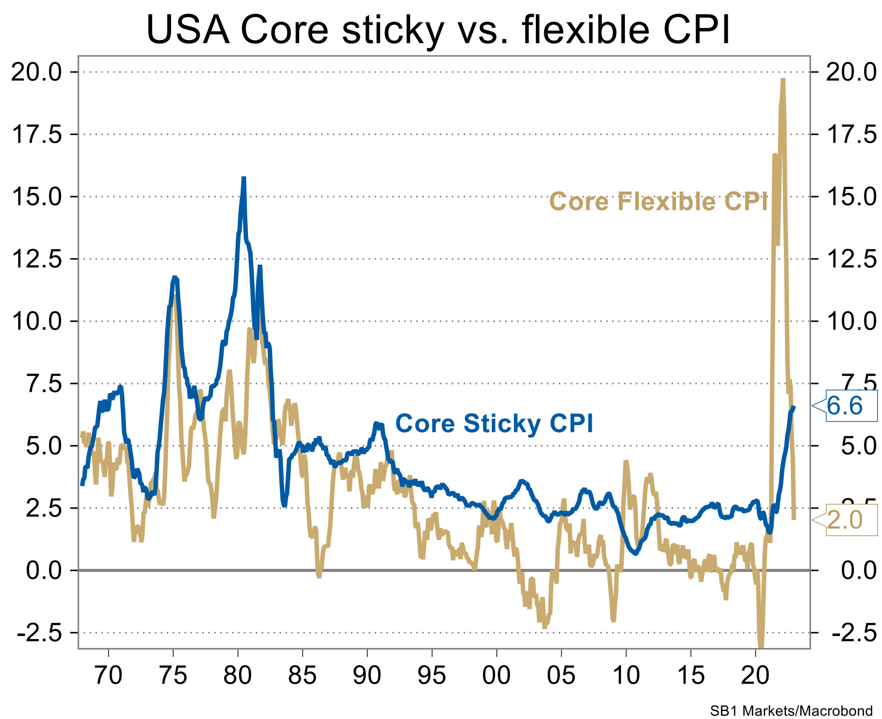
The trimmed median CPI inflation sharply down too

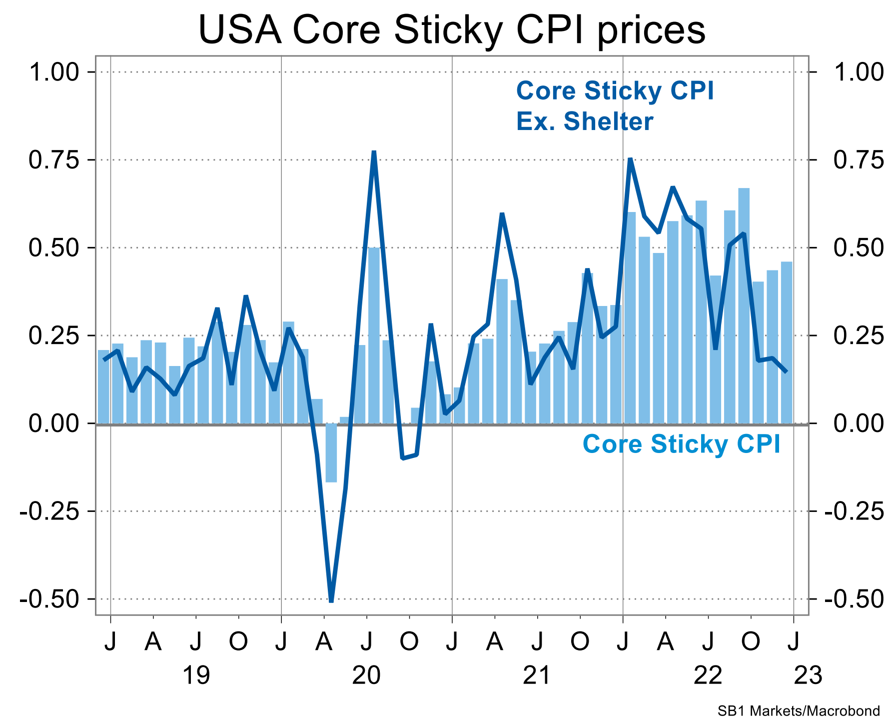


- The Cleveland Fed **trimmed median CPI** is up at a 5.5% pace over the past six months, down from 6.3% in November – and from the peak at almost 8%
- Dallas Fed's **trimmed mean PCE** was up 4.7% in November, down from the cycle peak in October

Flexible prices are coming down rapidly, *as are sticky prices ex. shelter*

Sticky prices (90% of the CPI) are up 6.6% y/y. However, excluding shelter, sticky prices rose just 0.1%

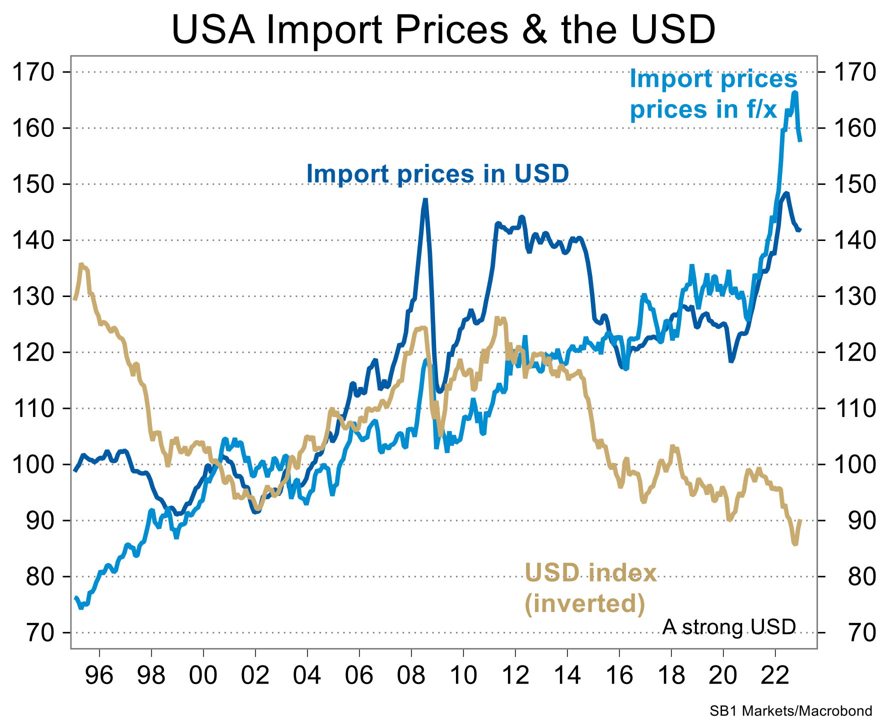


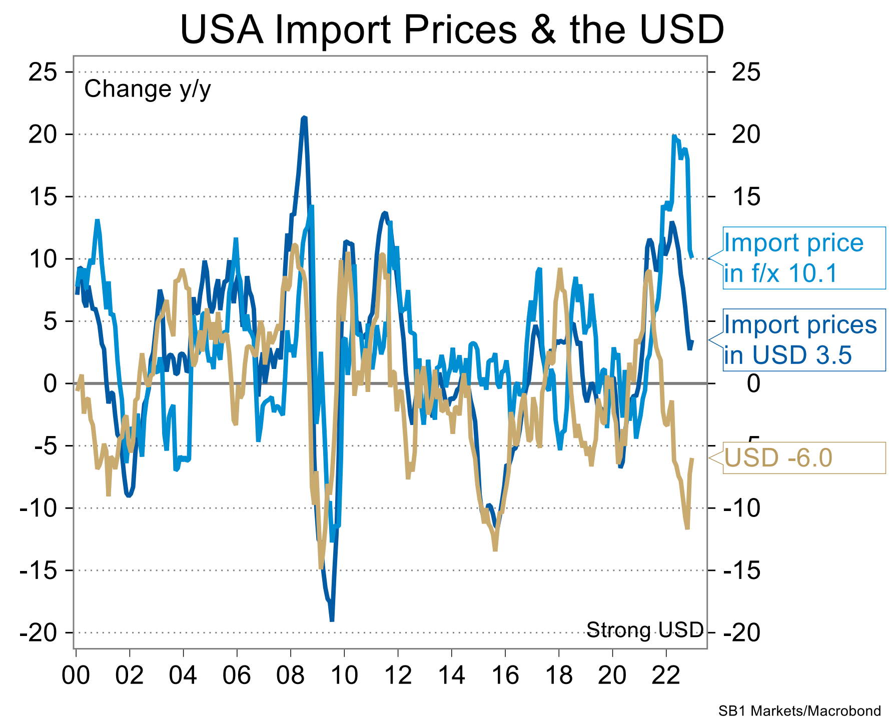


- Almost all of the initial lift in core CPI was due to prices of goods & services that often fluctuate, with rapid price increases now followed by deep price cuts. These prices are '**flexible'** and represent some 10% of the core CPI. The core flexible CPI is up 2.0% y/y, down from almost 20% at the peak!
- The **sticky components** (90 % of the core CPI) are up 6.6% y/y, due to the surge in housing rents

Import prices rose in Dec but the trend is down, even if the USD is down

Import prices rose 0.4% in December, and by 0.8% ex. petroleum, expected <u>down</u> 0.3%. Prices are still up 3.5% y/y

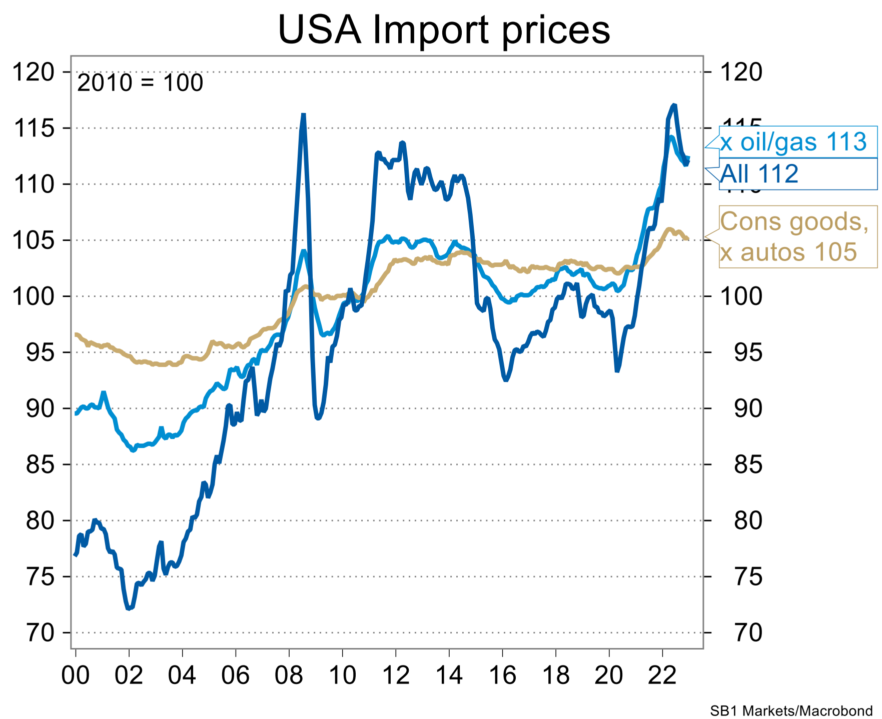


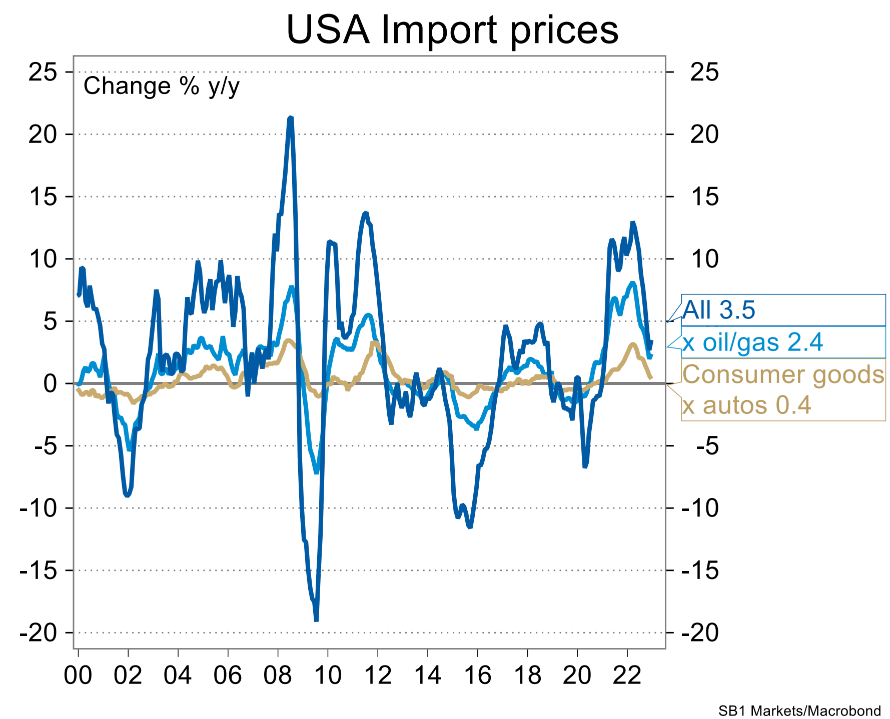


- Over the past year, the USD is up 6% even after the recent depreciation
- Measured in f/x, import prices are up 10%, down from 20% at the peak
- However, prices have fallen both measured in USD and in f/x since April/June – and we expect them to continue downwards. Prices were up 13% y/y at the peak last March

Prices are up 2.4% y/y ex oil/gas, while consumer goods ex auto are up 0.4%

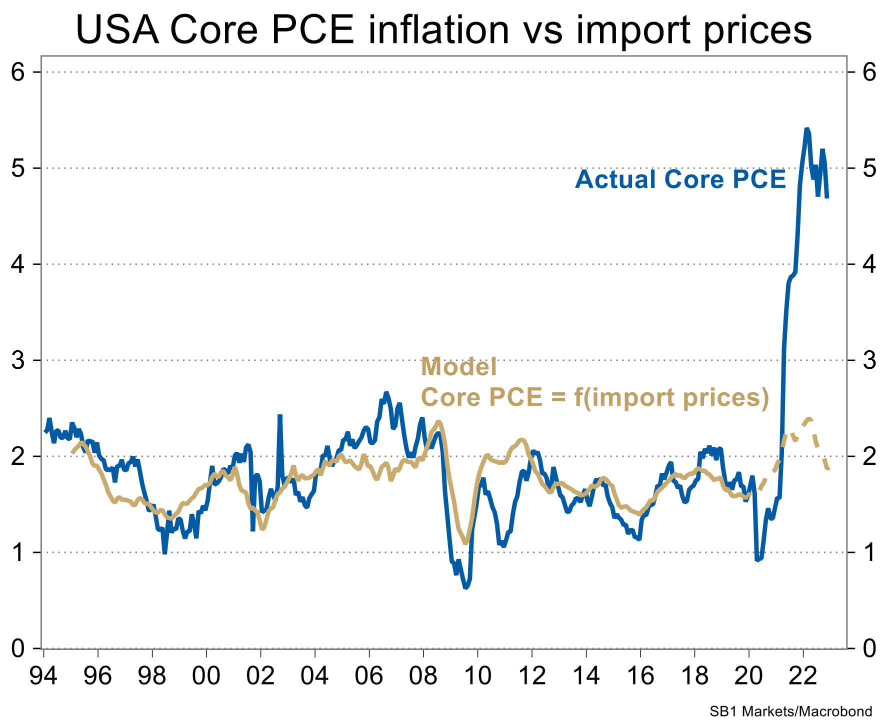
Consumer goods prices have been falling since last spring as well (in USA), and they were flat in December





Import prices are correlate to domestic inflation

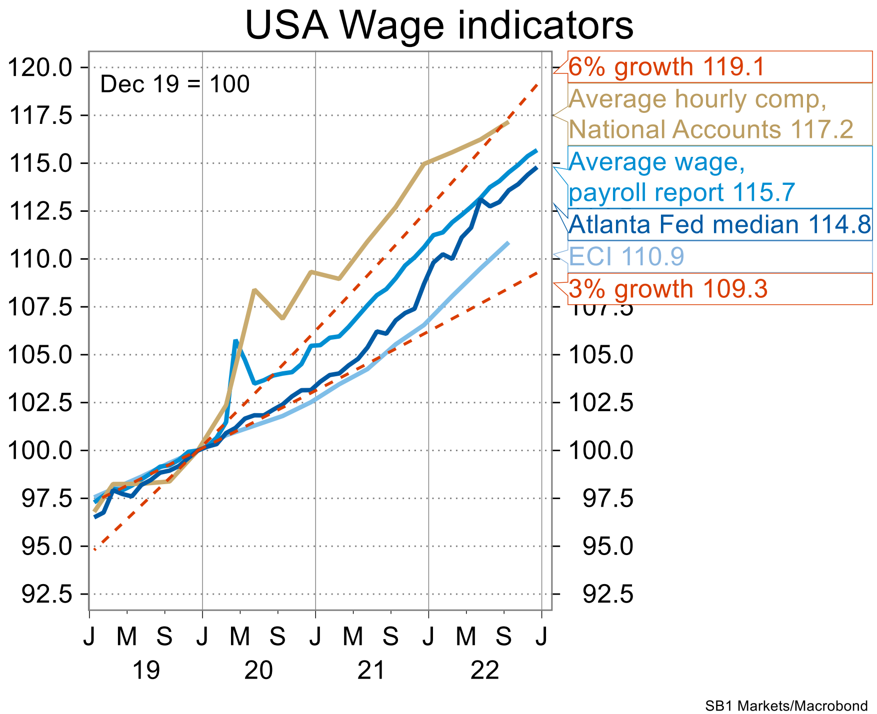
… But they are not causing inflation, they are driven by many of the same factors

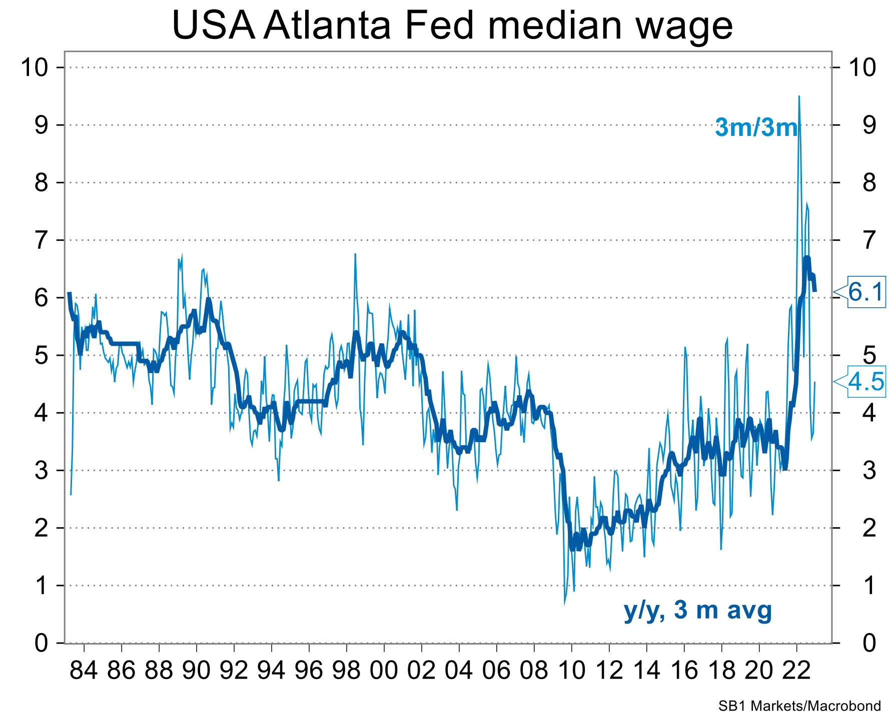


- … and the recent surge in US inflation cannot be explained by the increase in import prices – as such surges are rather normal

Atlanta Fed's median wage tracker has also peaked

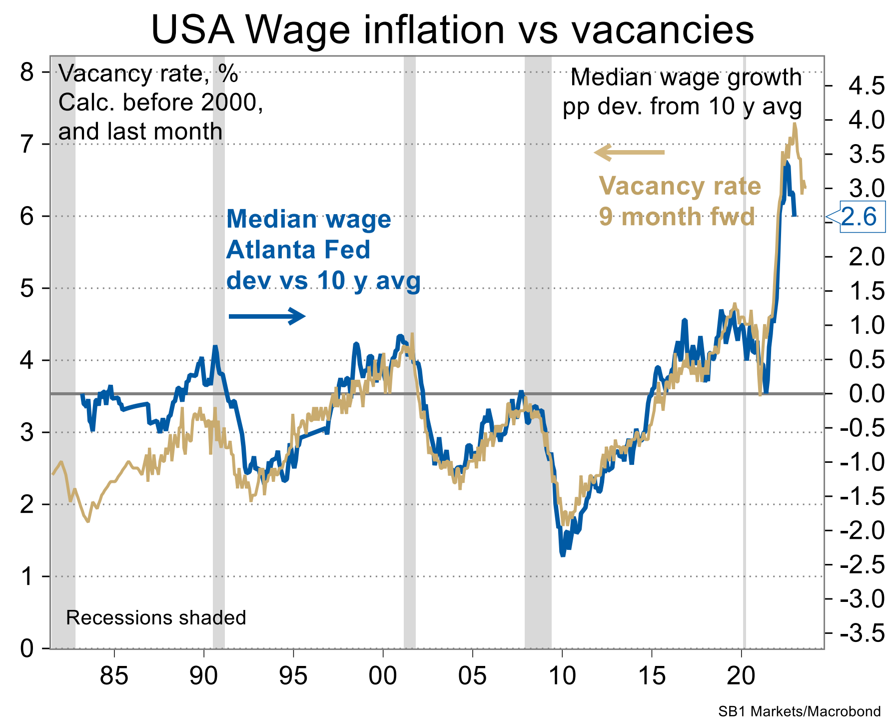
Even if the annual rate remains above 6%, underlying growth has slowed to below 5%. Still some 1.5+ pp too much





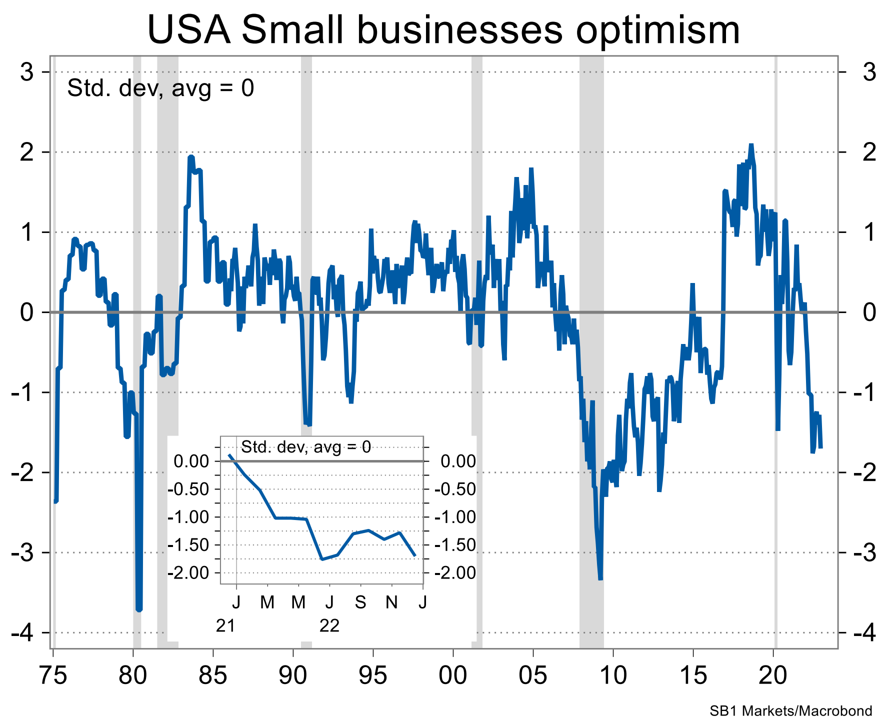
- **Wages** rose some 0.4% m/m in December (our calc.)
- The non-smoothed annual rate fell 1 pp to 5.5% (due to a rapid lift in wages in December last year), but even the 3m smoothed rate declined 0.3 pp to 6.1%. The peak was at 6.7% in June/July last year
- This series is somewhat volatile but the underlying trend has fallen to 4.5% – 5% recent months

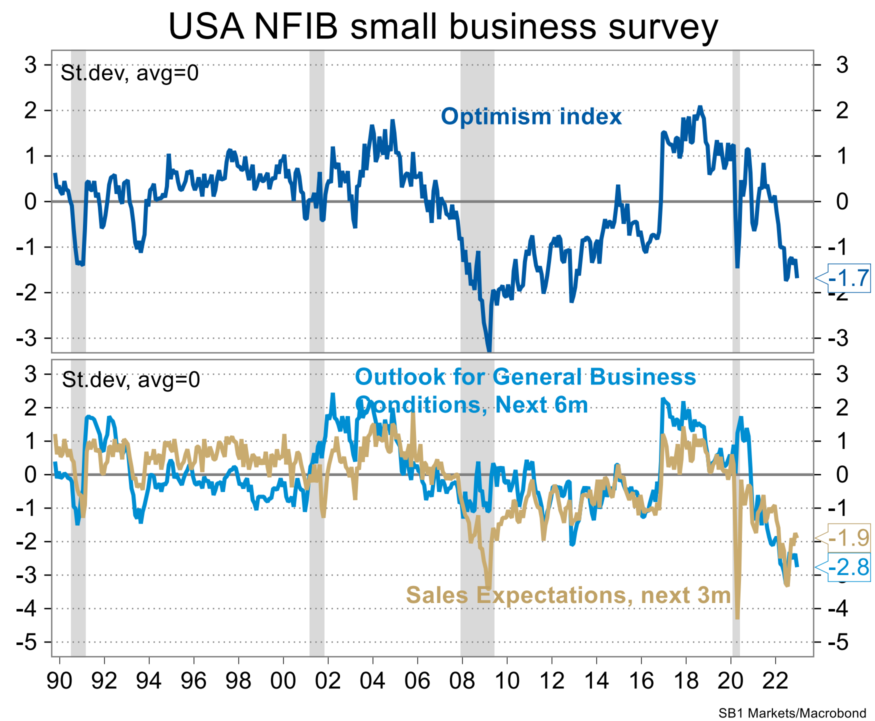
Wage inflation is slowing, but remains too high



SME optimism weaker in December, and price plans are slashed!

Even before poor sales have become a problem!! A real 'Goldilocks' news!



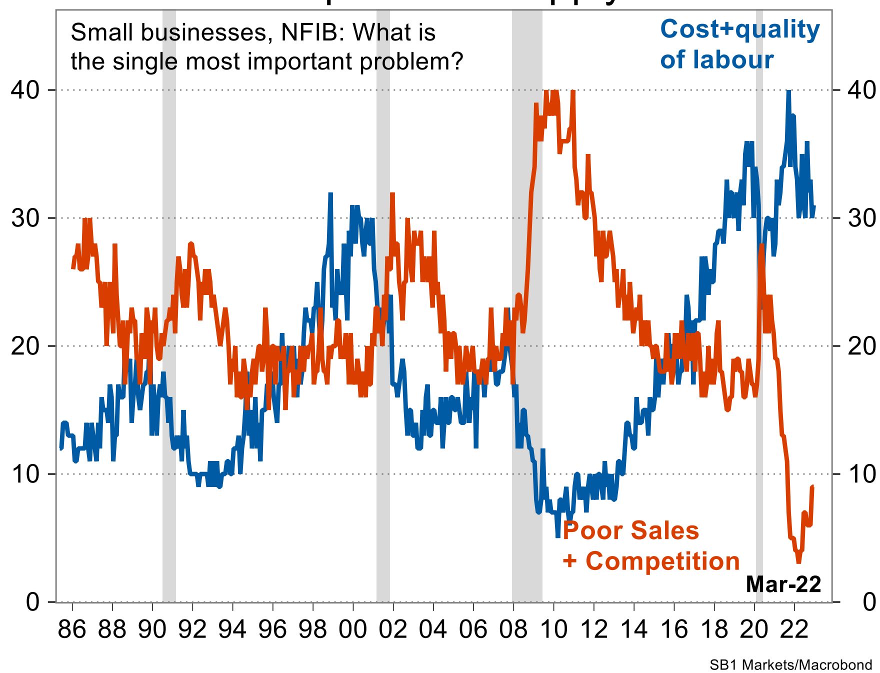


- The **NFIB optimism index** has been rather stable at a low level recent months. In December, the index fell to 1.7 st.dev below average from 1.3 st.dev below avg. **The outlook for the next 6 months** also fell, to 2.8 st dev below average (it was lower in May-July '22)! **Sales expectations** fell marginally as well, to -1.9 st.dev below par
- **Inflation, lack of qualified labour and labour costs** are still the main worries for the SMEs. However, some more companies report that **competition** is a worry, but the share is still very low
- The share of companies that **plans to lift prices** fell sharply in December, by 10 pp to 24%, still somewhat above the average at 21%. But the decline was the 3rd largest ever! Even if companies revised their compensation plans upwards, this is really goods news for the Federal Reserve, as price plans have more or less normalised before companies start complaining about their sales (they are still rather worried for future sales, though). Higher wages and lower prices are not good new for profits, of course

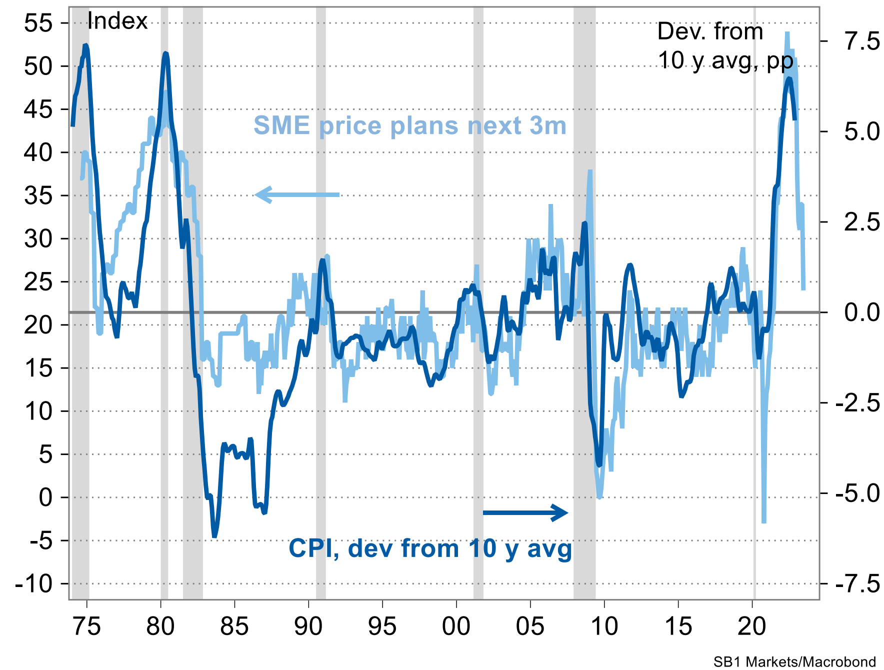
Price increase plans are 'collapsing', the 3rd largest drop ever!

Even if sales/compensations are not yet the problem, lack of labour still is!

USA What's the problem: Supply or Demand?



USA Small Businesses Price Plans

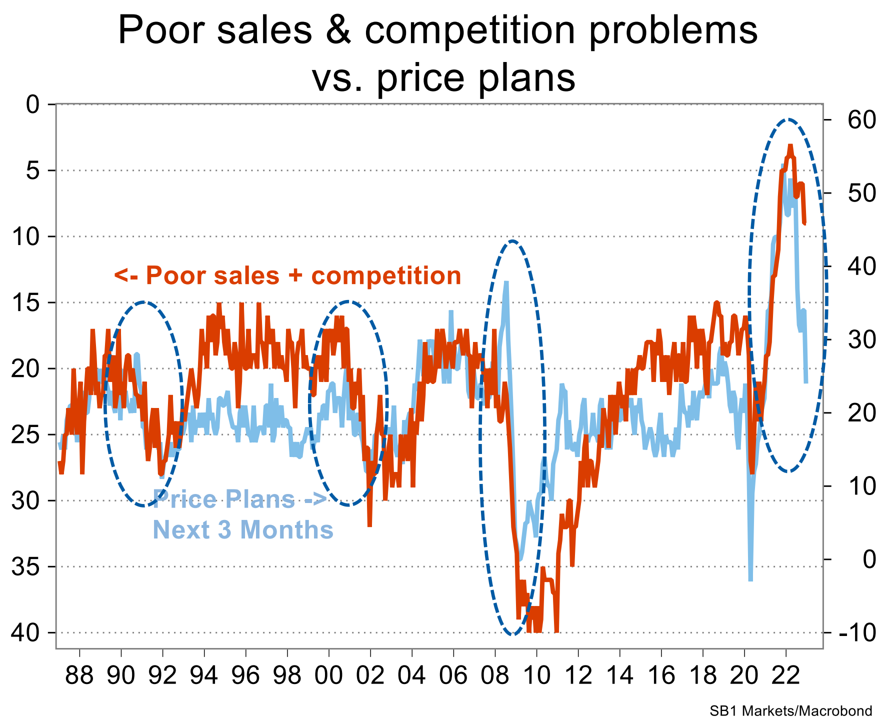


- **The 'gap' between supply and demand concerns** is still very large, but it is now heading down
- Very few companies report **poor sales** as a problem, somewhat more complain about **competition**. The total share is up from March, and increased further in Dec. **Cost & quality of labour** are stated as the most important problems for a much higher share of companies than normal. However, the share has fallen somewhat from the peak (but not further in December) – and compensation plans were revised up!
- The share of **companies that plan to lift prices** has fallen sharply from the peak and fell 10 pp to 24% in Dec, not far above the average at 21%! The decline was the 3rd largest ever! This is really encouraging new for the Fed! <u>Price plans are coming down before sales have become weak! This is rather unusual, check next page</u>
- We still expect the sales/competition to become the major worry for small businesses – but are less sure than before this report!

SpareBank 1 MARKETS

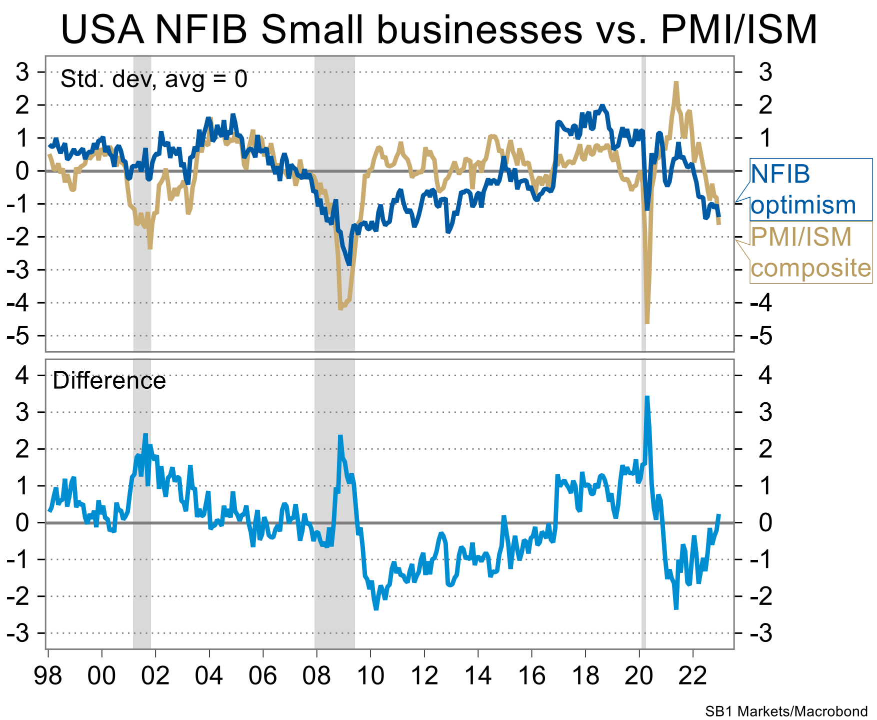
Prices plans have retreated, before poor sales has become a problem

… which is not the norm!



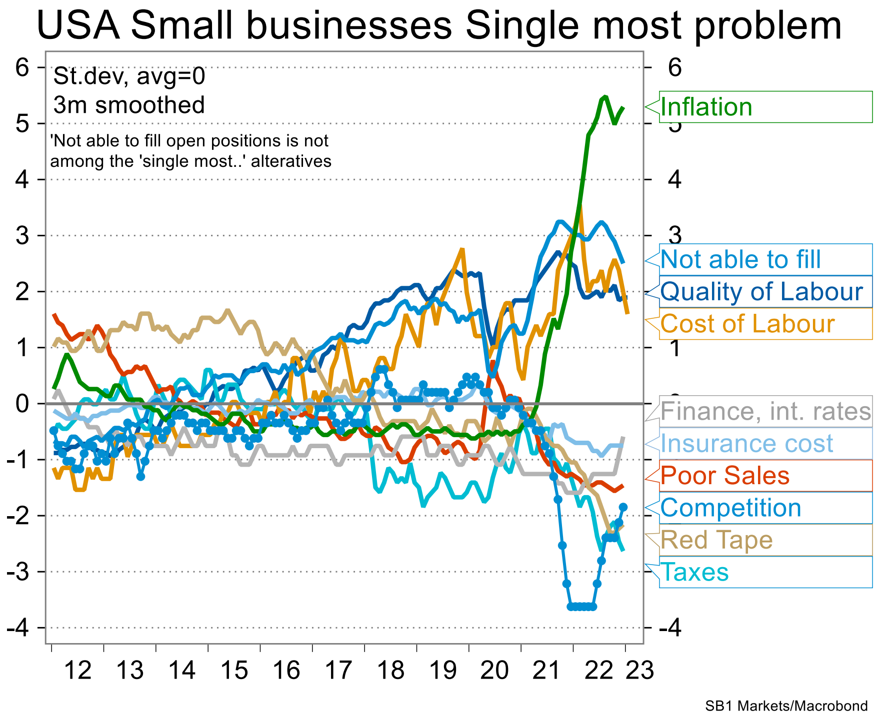
Large and small businesses are now better in sync

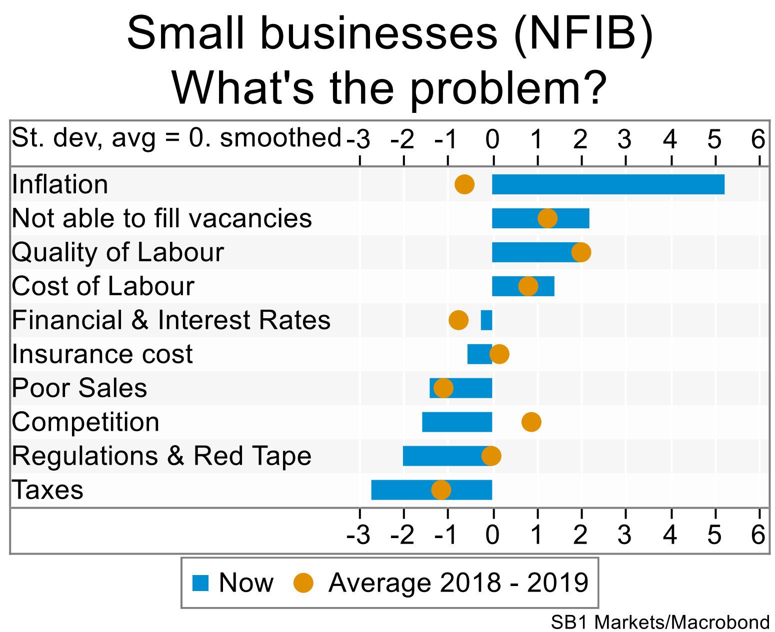
… As it turns out that the SME’s were closer to the ball



Inflation is the biggest problem (even if companies are 'selling' inflation)

But the cost of labor and not able to fill vacancies are less of a problem now than the recent months

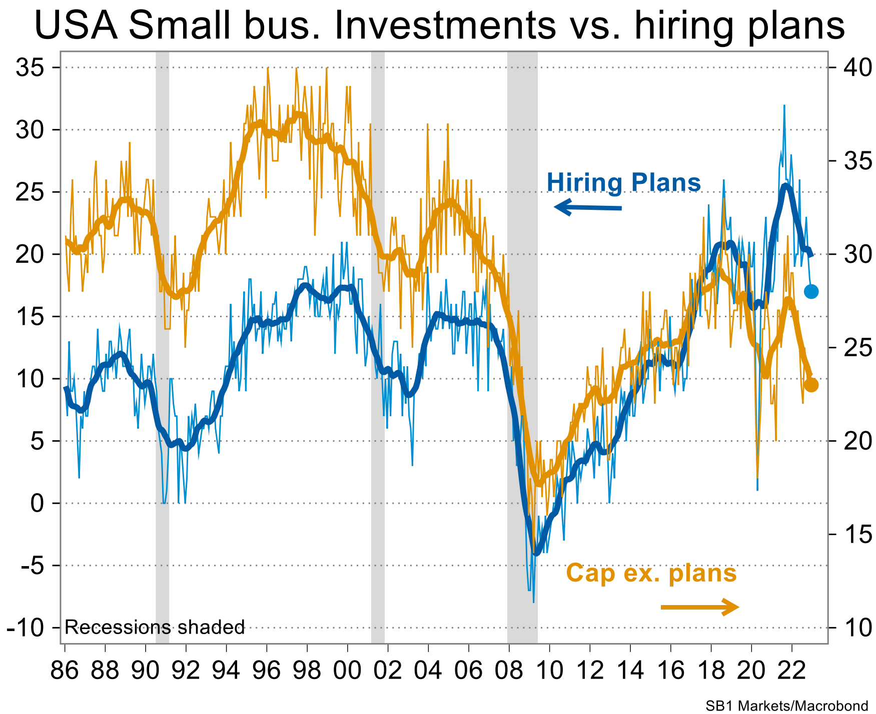


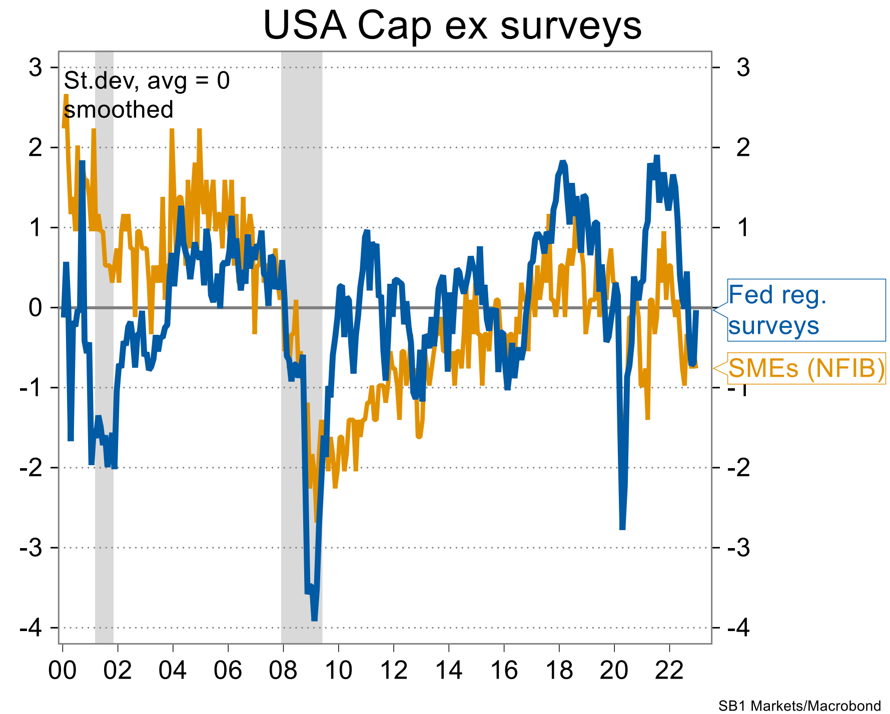


- Companies still report they are constrained from the **supply side**, not from the **demand side**

In the charts above, we have included the 'Not able to fill open positions' data from the survey, but this is (rather strangely) not an alternative in the single-most-problem question in the survey. We still show it in the chart

Small businesses revised their hiring and investment plans down, again…

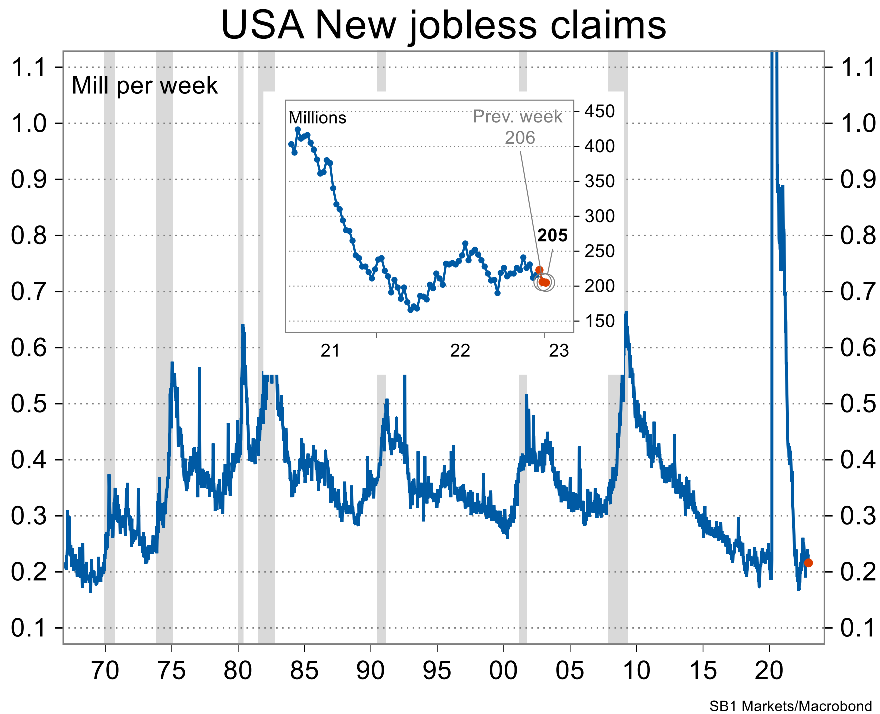


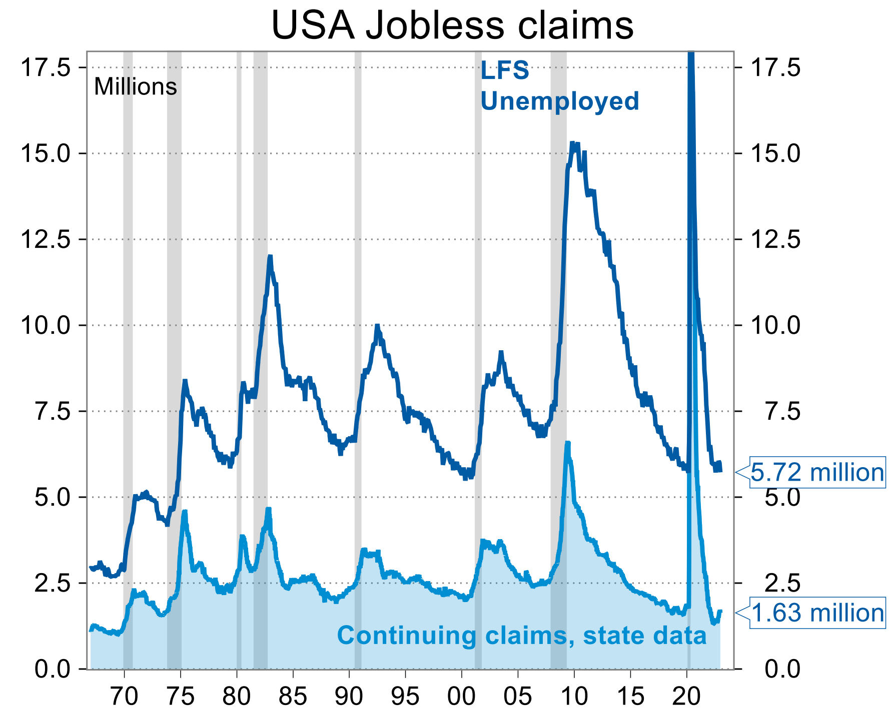


- The NFIB survey report of investment plans far below average
- Other (regional Fed) investment surveys have also come down from the top, to below an average level

The inflow of new unemployed remains a trickle, unch. at 205’ last week

... 9’ below expectations

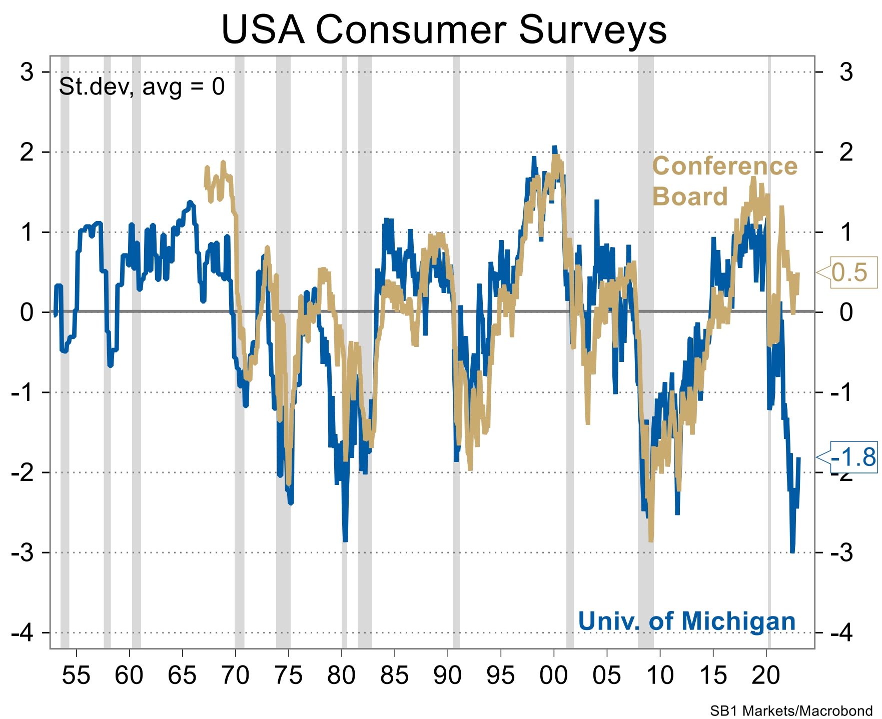




- **New jobless claims** decreased down 1’ to 205 last week
- **Continuing claims** fell by 63’ to 1,630’ in week 52. The trend is slightly upwards but the level remains very low still
- Both still indicate a **tight labour market** – a labour market that is far more resilient than we and probably also the Fed had envisioned, given higher interest rates, record-low consumer sentiment, and falling orders (according to surveys)

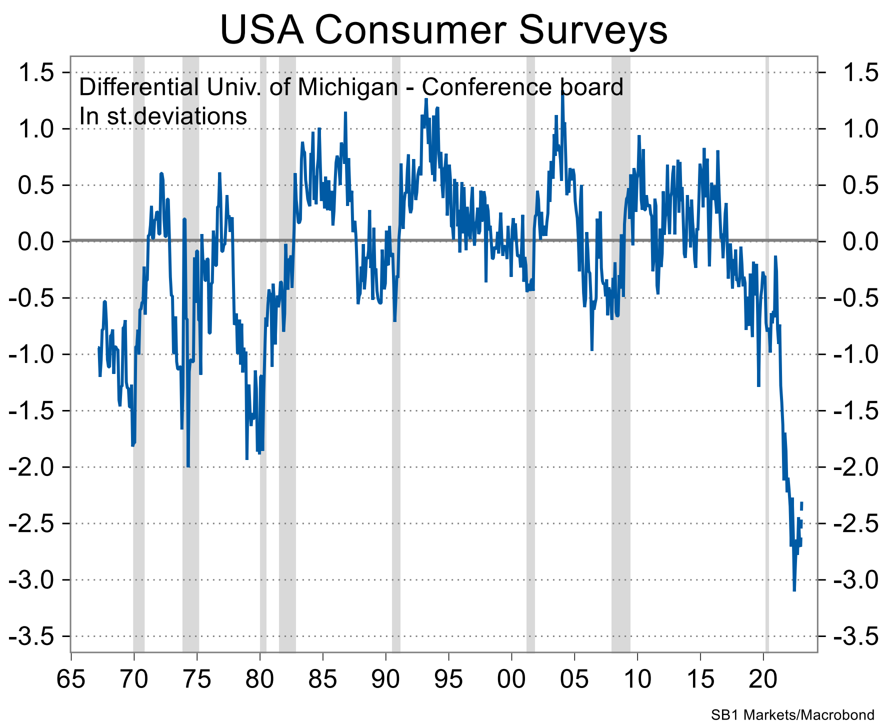
Univ. of Mich. sentiment further up in early January

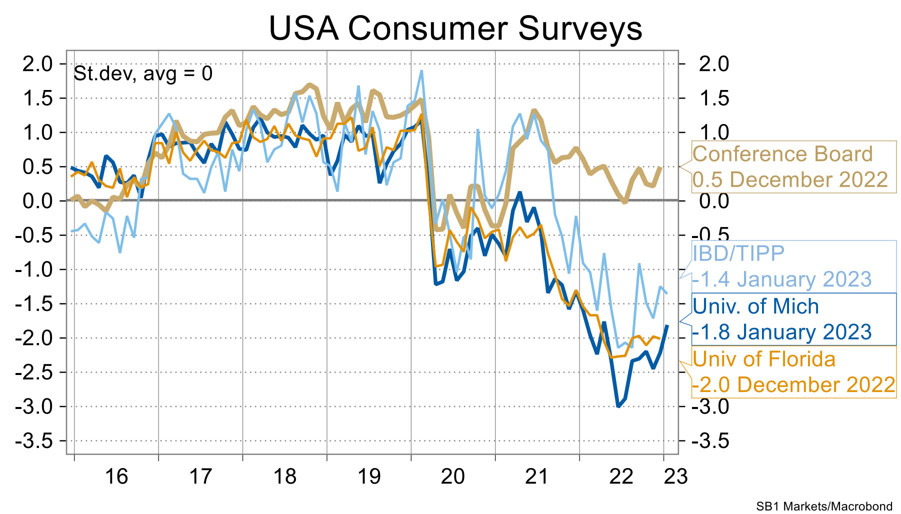
The sentiment index is still at a low level, 1.8 st.dev below average. All other surveys have turned up



- **University of Michigan's consumer sentiment** climbed 4.9 p to 64.6 in the first part of January, expected 0.8 pp. The level equals 1.8 st.dev below average, after a 0.4 st.dev lift. The bottom was in in last June, at -3.0
  - Both households' assessment of the current situation and expectations fell in November, expectations the most
- **The 3 other consumer surveys** all turned up recent months
- **Short-term inflation expectations** fell significantly, for the coming 12 months to 4.0% from 4.4% in November, and from 5.4 at the peak. The 5y expectation rose 0.1 pp to 3.0%
- **The risk:** The UM survey is still at a very low level, and is often an early bird in the cycle

All surveys up recent months, most are still on the weak side

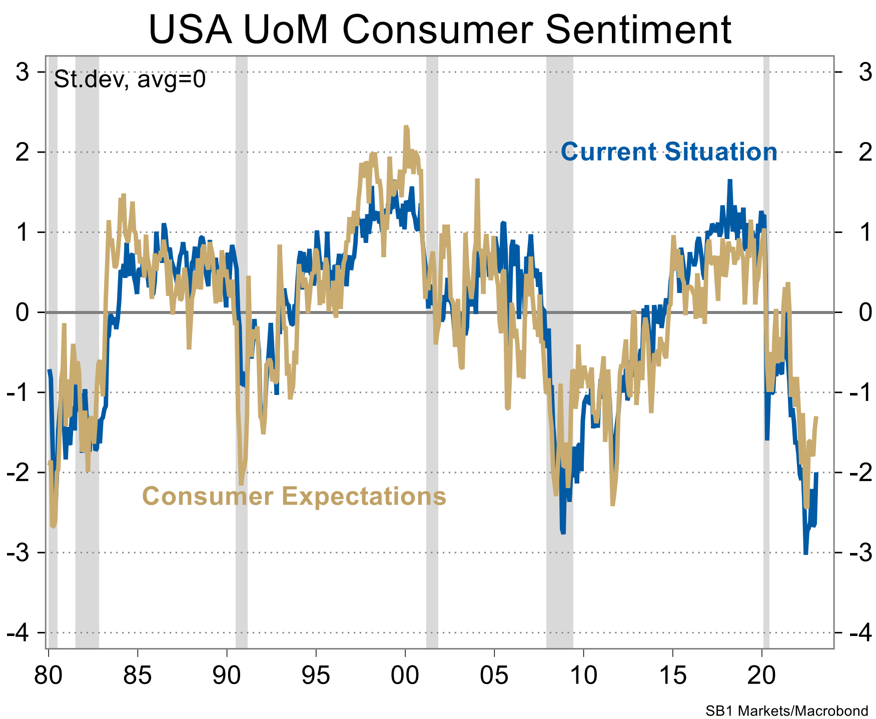


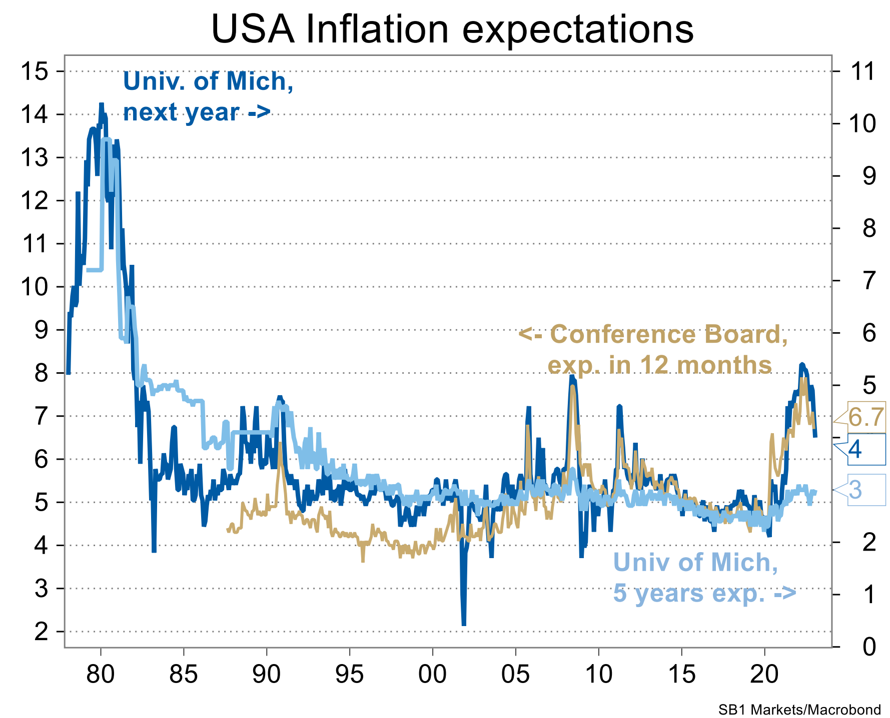


- Quite often, the UM survey has been the canary in the mine vs. recessions, it yields earlier than Conference Board's survey. Now, however, the UM is turning upwards, before CB's survey really fell
- Both IBD/TIPP consumer survey, Univ. of Florida's survey are 1.4 – 2.0 st.dev below par

Univ. of Michigan: Both current situation & expectations up in January too

Inflation expectations in sum down. The near term outlook is getting better, households say

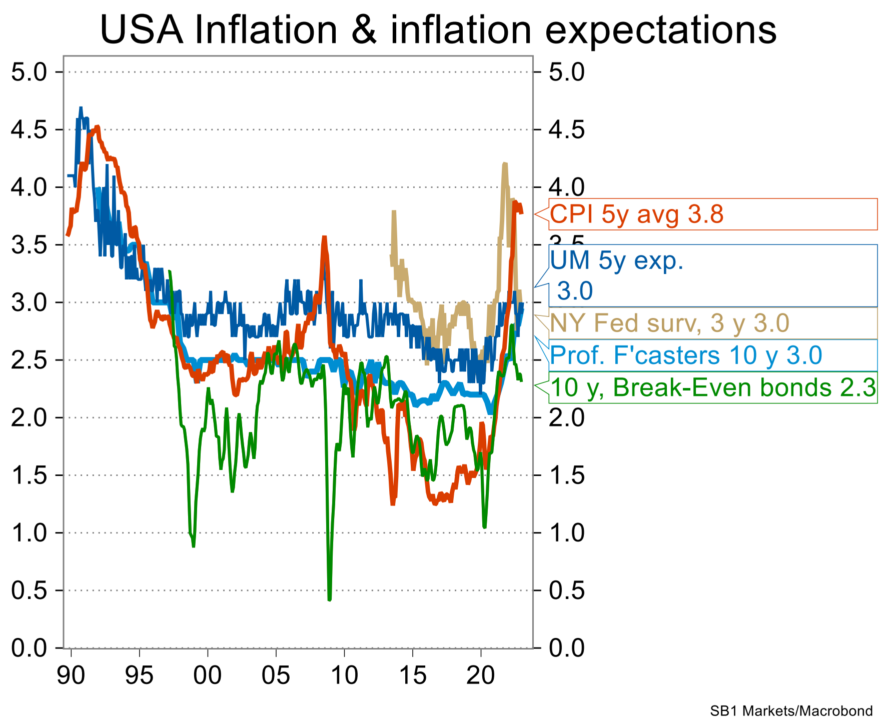


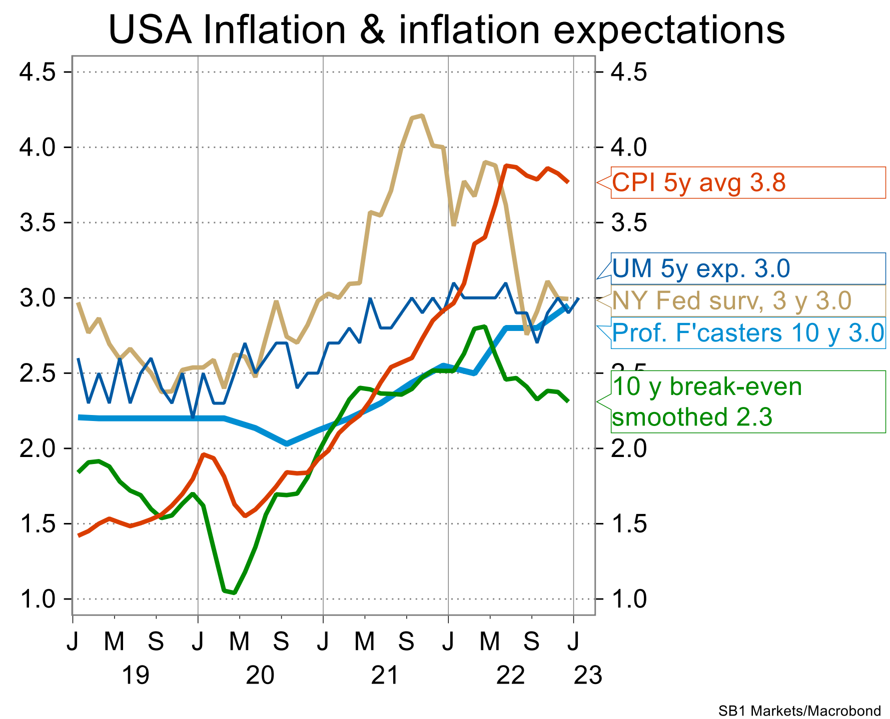


- **12 m inflation expectations** declined to 4.0% in January, from the initially reported 4.6% a month ago
- The peak was at 5.4%, last March
- **5 y inflation expectations** were up 0.1 pp to 3.0% - and they have been close to 3% over through 2022 – and some 0.5 pp higher than during 2016 – 2021 – but in line with expectations over the preceding years
  - The 3.0% is just 0.1 pp above the average over the past 10 years, not that much given the current rate of inflation

Professional forecasters have revised their 10y CPI est. to 3%

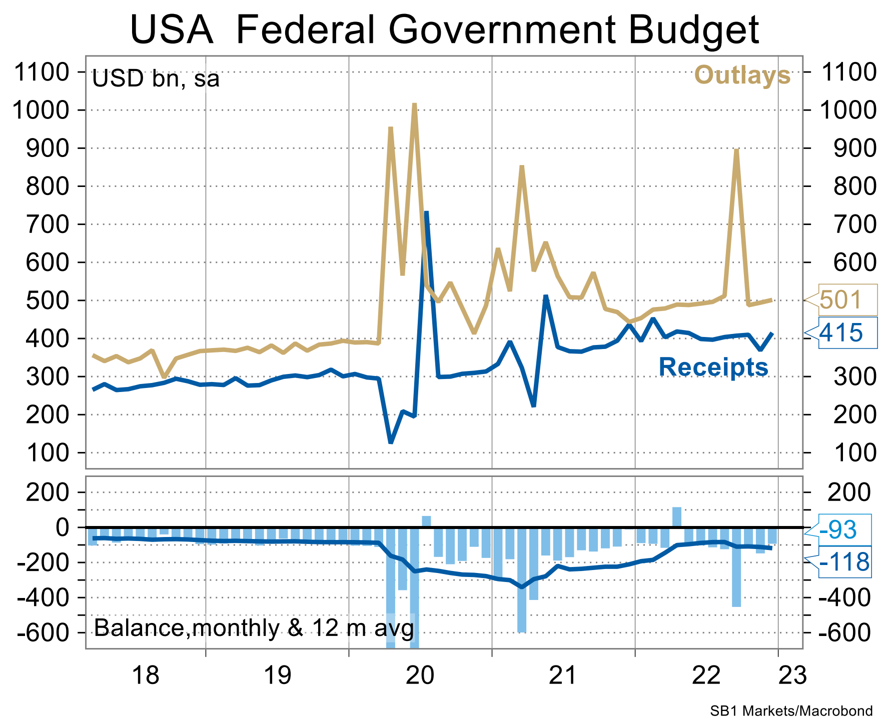
In Q4, professional forecasters upped their quarterly forecast by 0.2 pp to 3% avg. 10 y inflation. Was at 2% in 2020

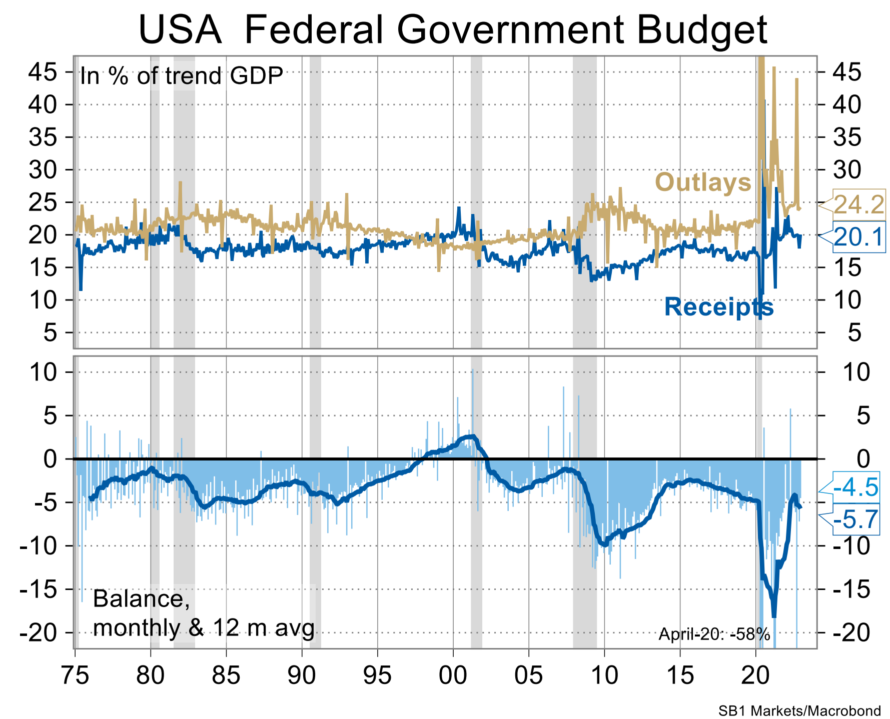




The budget did not reach balance – and now it is too late?

A slowing economy will not strengthen the budget – and the deficit will widen again

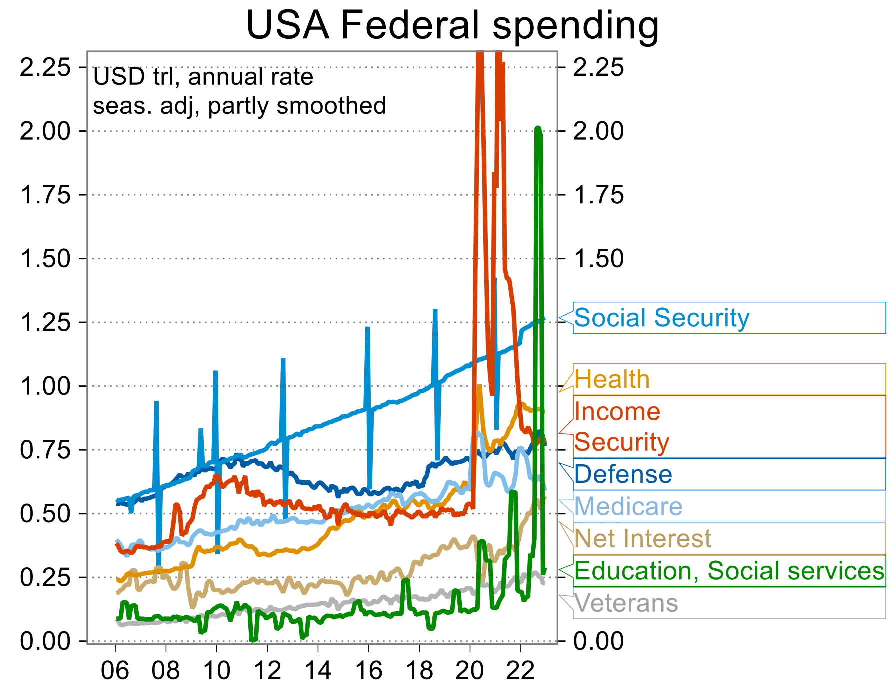




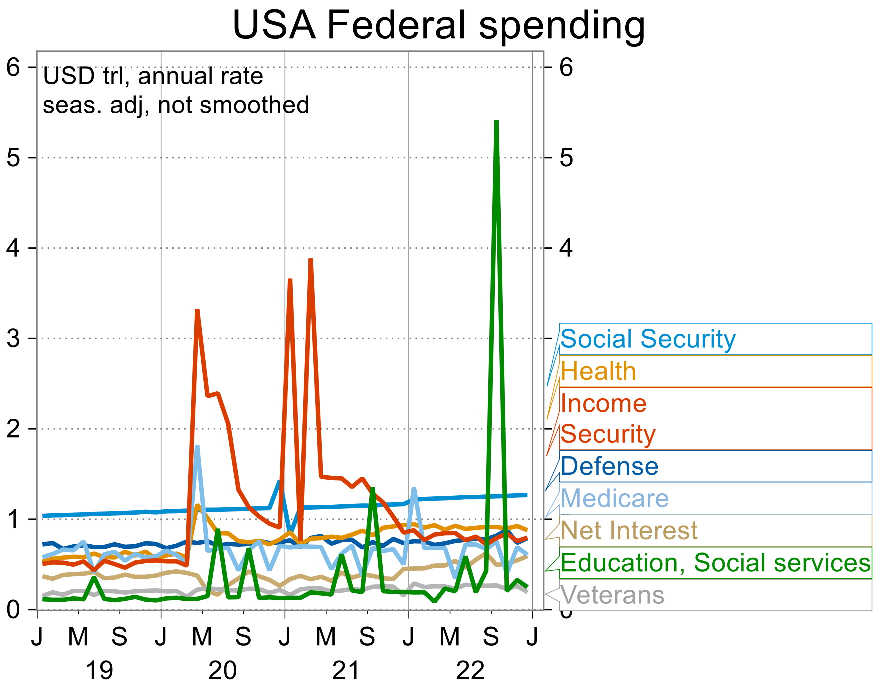
- **Federal expenses** fell rose just marginally in December The trend is clearly upwards. Spending equals 24% of GDP, up from 21% – 22% before the pandemic
- **Federal receipts** have flattened through 2022, even if growth in nominal GDP has been strong. Receipts equals 20% of GDP, above the 17% level ahead of the pandemic
- The actual **deficit** was USD 85 bn in Dec, expected 70, bn - or USD 12 bn seasonally adjusted, which is 4.5% of GDP. Over the past 12 months the Federal deficit has equalled 5.7% of GDP. Before corona, the federal deficit also was close to 5%. In a booming economy, the budget should of course have been in surplus, now even more than before the pandemic

Spending has normalised post the student debt relief lifted spending in Sept

Net interest rate payment have increased by almost 50%, equalling 1.5% of GDP. And more to come!



SB1 Markets/Macrobond

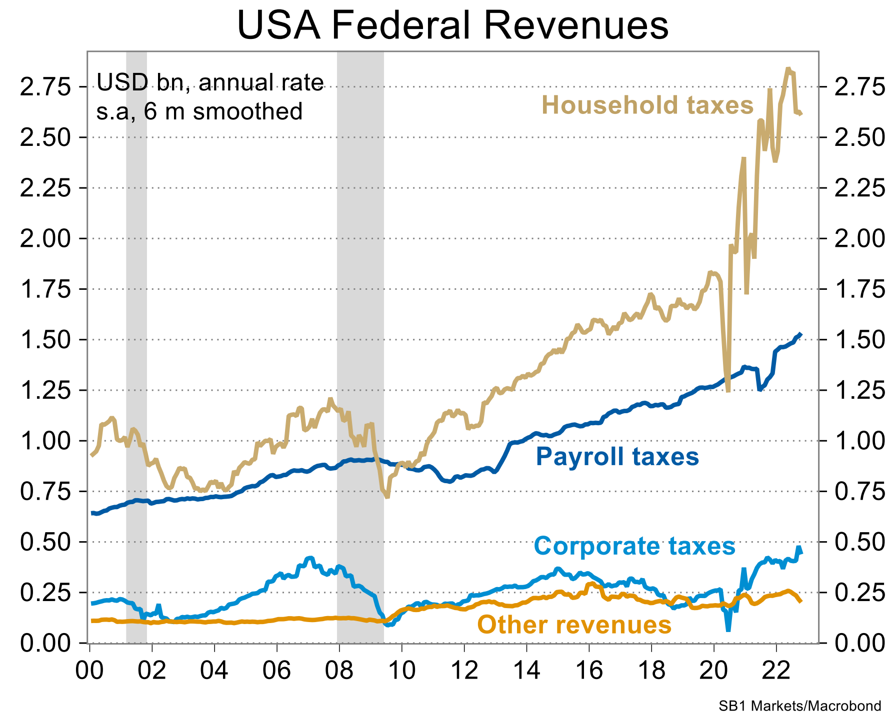


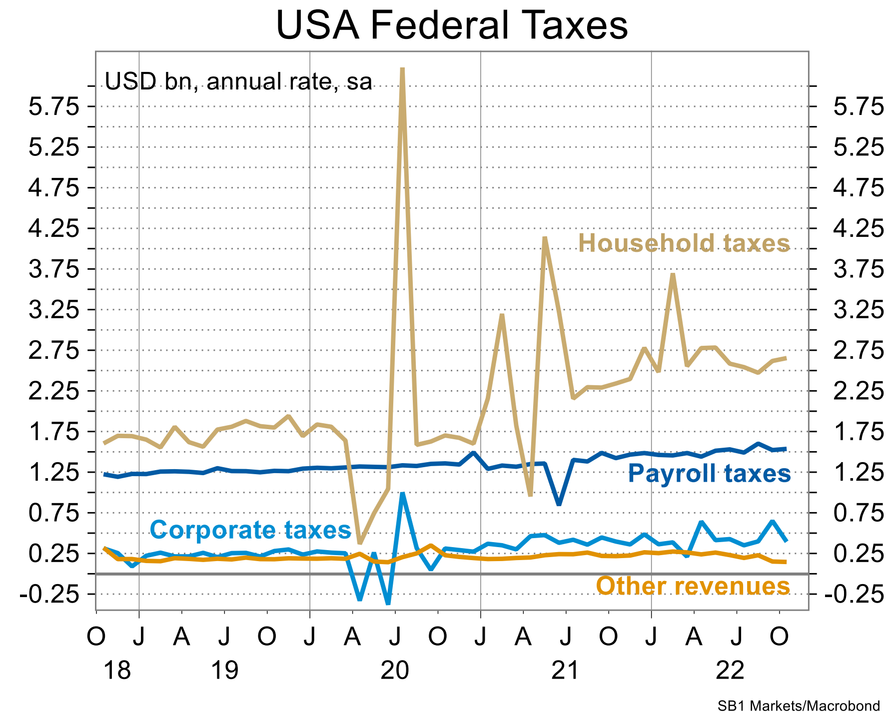
SB1 Markets/Macrobond

- Most components are trending up
- Interest rate payments will increase substantially from the present level, even if bond yields do not climb further form here – since new (and refinanced) debt have to pay current yields, which are higher than average yield on maturing bonds
- Both income security and 'other spending' are well above the pre-pandemic level. Health spending is sharply up too

Tax revenues are remarkably higher than before the pandemic

Especially taxes paid by households (+60%) and corporates (50%+)!

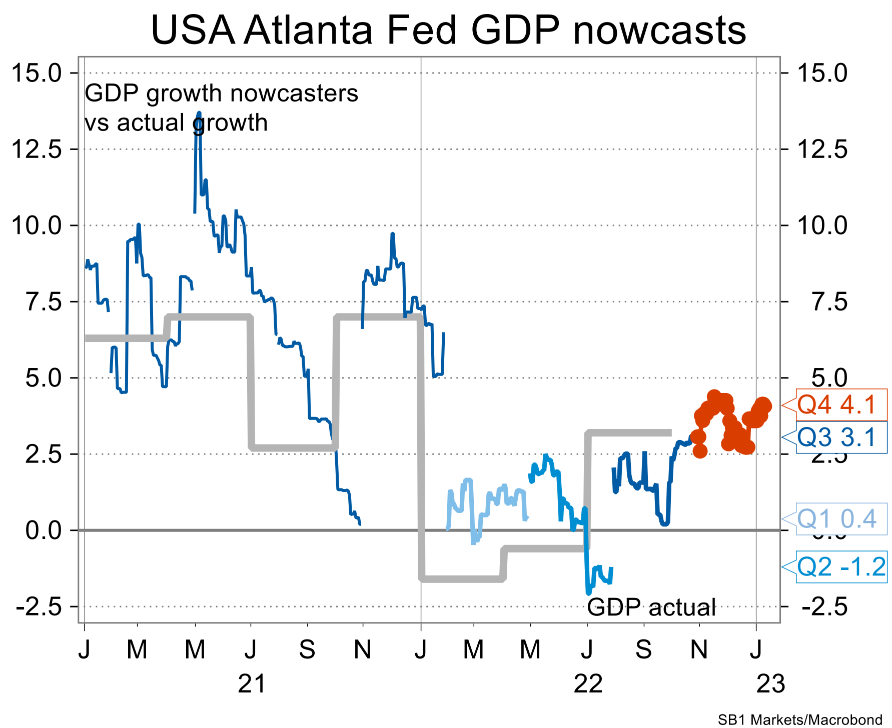


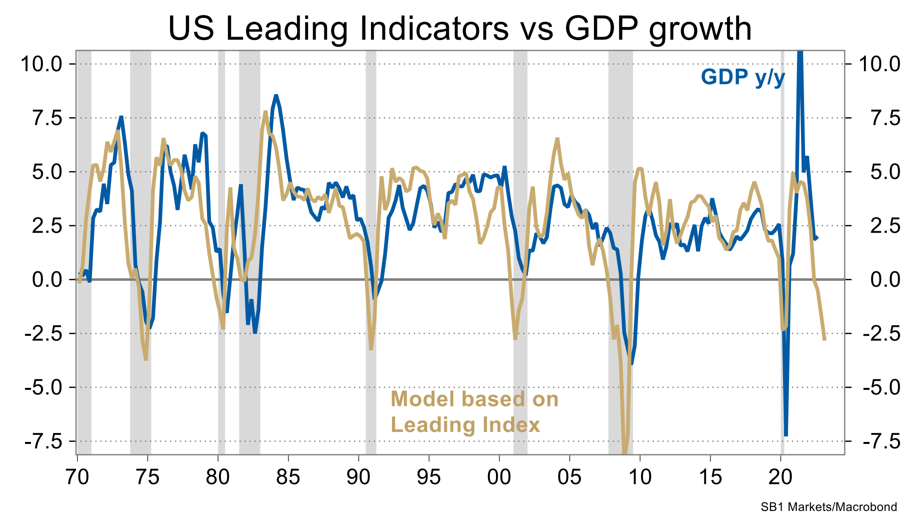


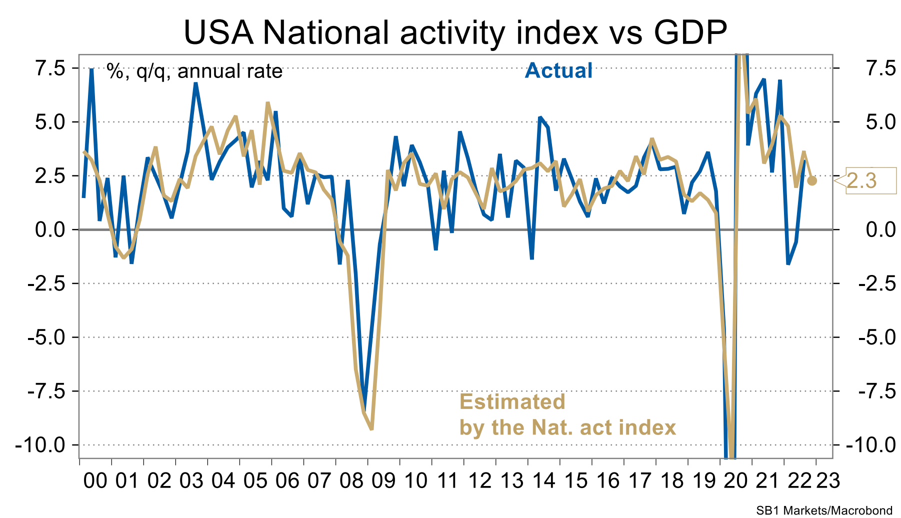
- And taxes have increased more than what could be explained by the surge in nominal GDP (due to the surge in inflation)

Atlanta Fed revised its Q4 GDP forecast up by 0.1 pp to 3.8%

By far the most upbeat among nowcasters. Leading indicators are signalling a decline in GDP before not too long

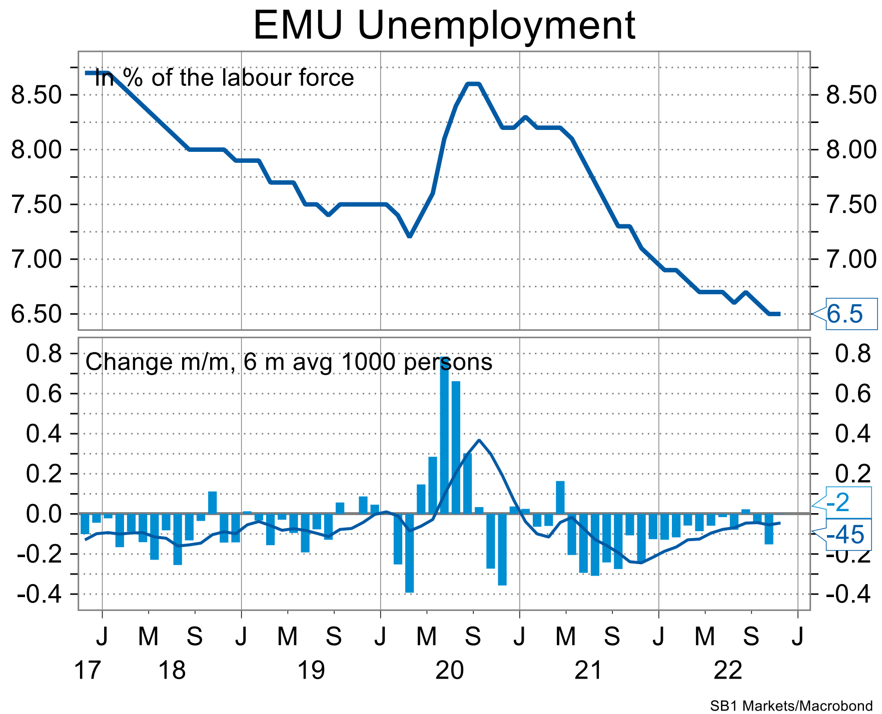


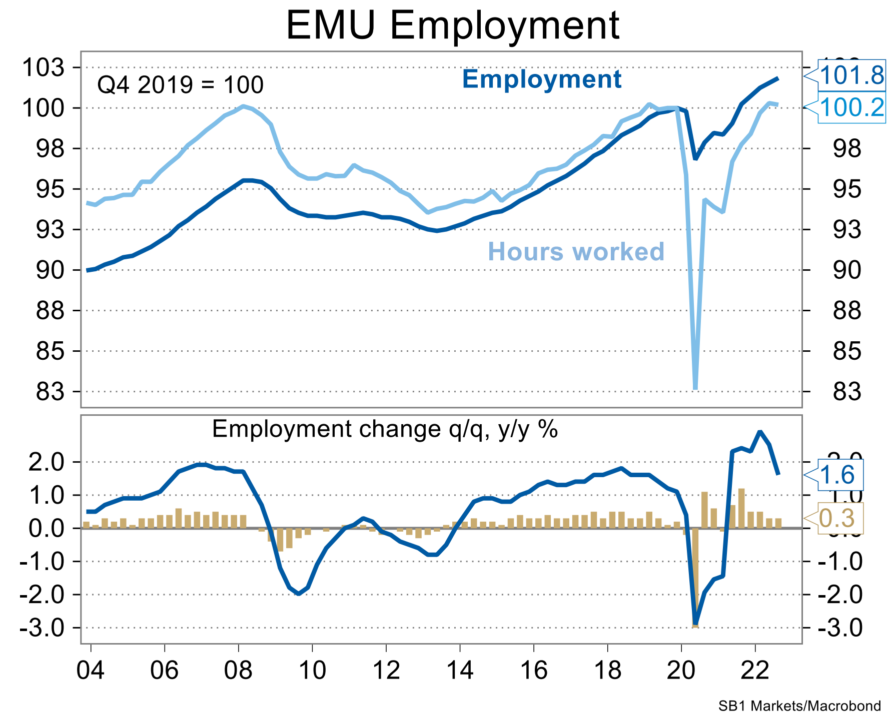




Unemployment stable at 6.5% in November, the lowest level since 1989

The no. of unemployed was unch. m/m, following a 45’ drop last month. Employment is still growing

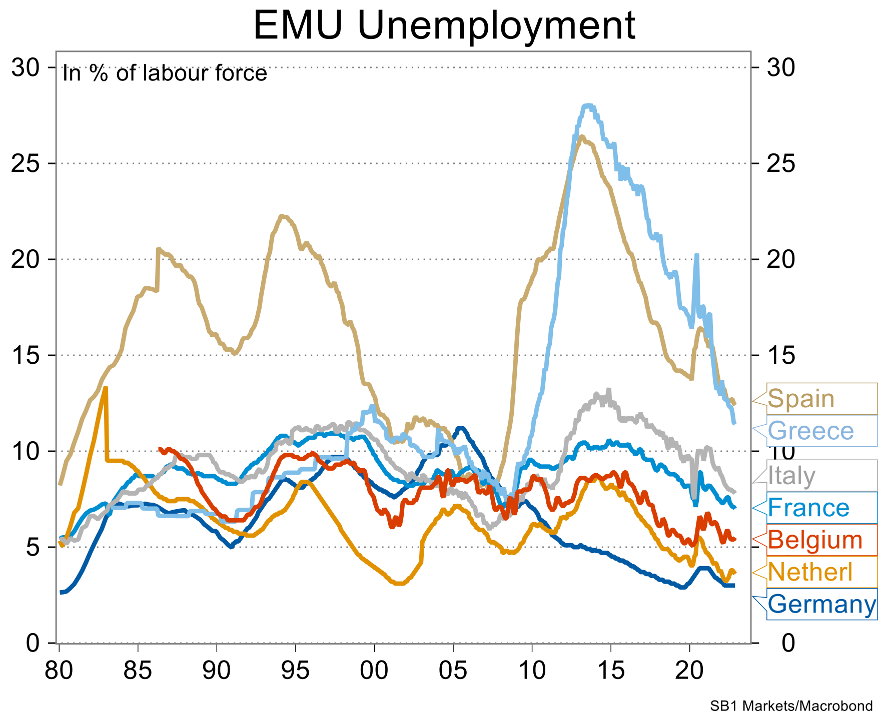


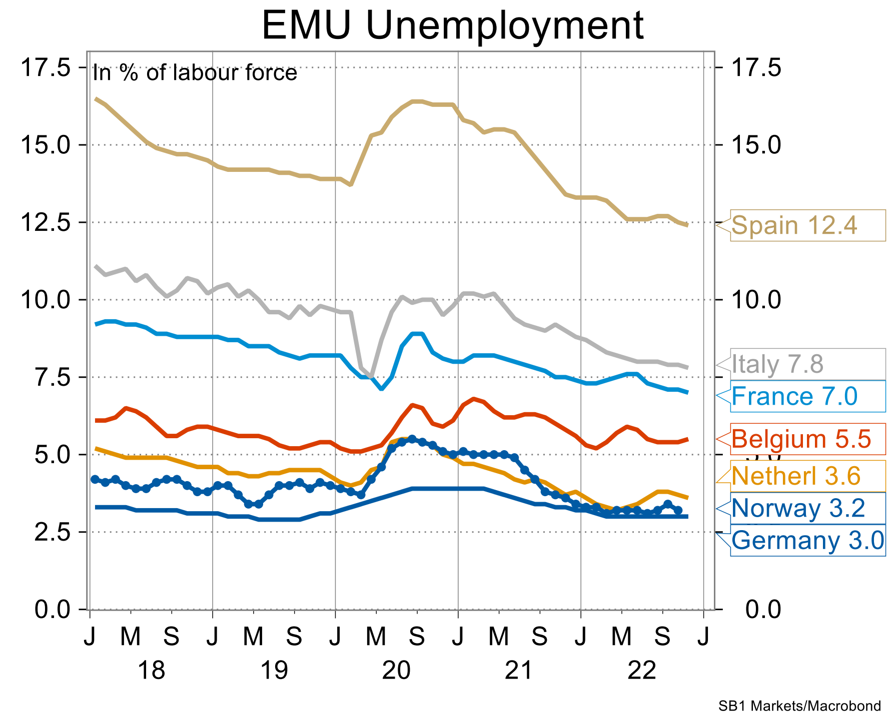


- **The unemployment rate** was unch. at 6.5%, as expected. The number of unemployed persons fell by 2’
- **Employment** grew by 0.3% in Q3 (not annualised). The employment level & the employment rate are both higher than before the pandemic
- The number of **unfilled vacancies** is still high, but seems to have peaked
- The labour market is no doubt still very tight – until further notice
- **Wage cost inflation** has not accelerated but a slowdown in productivity growth has pushed labour cost per produced unit upwards, to somewhat above 2%

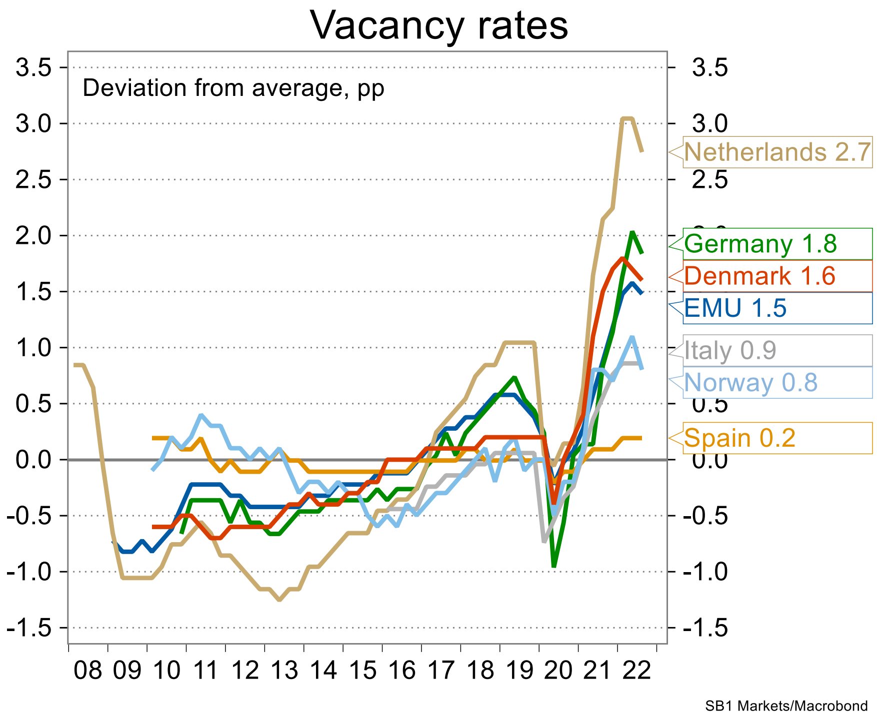
Unemployment is lower than normal everywhere

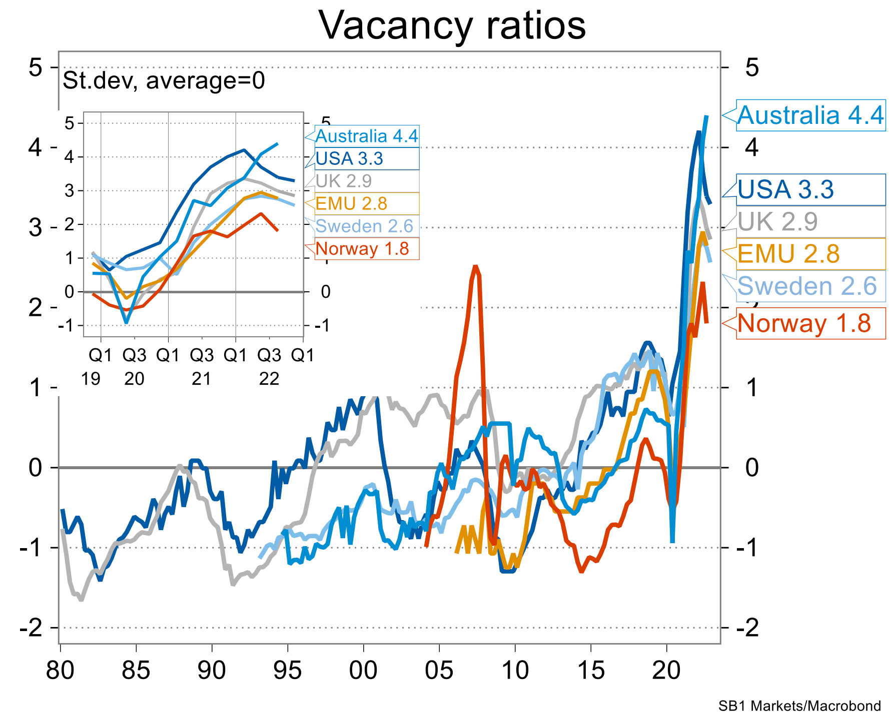
Unemployment in Belgium & Netherlands is marginally up from a local bottom, others are flat or are trending down





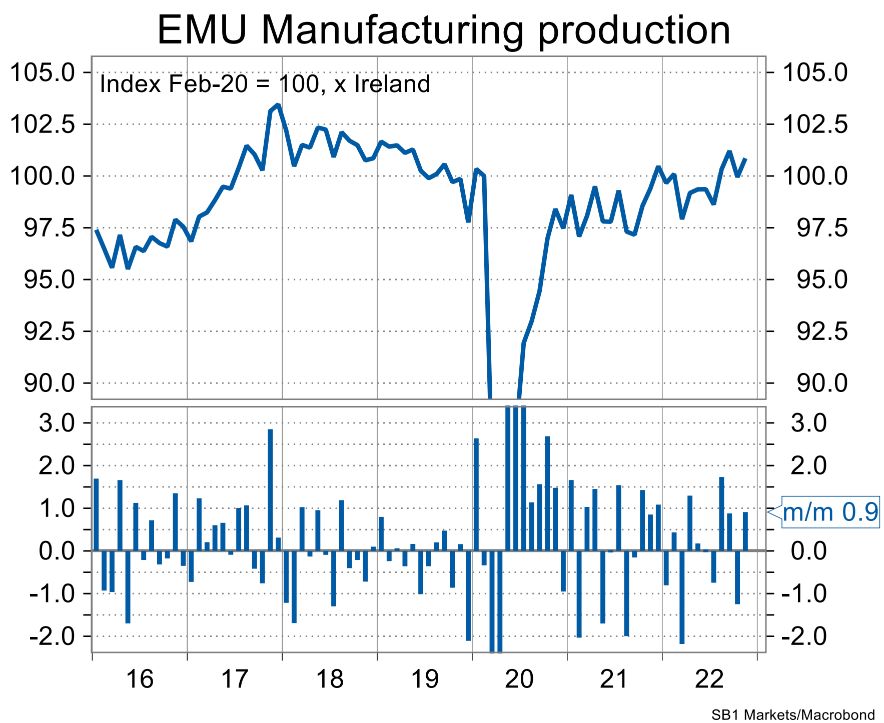
Unfilled vacancies have peaked most places – but the rates remain very high

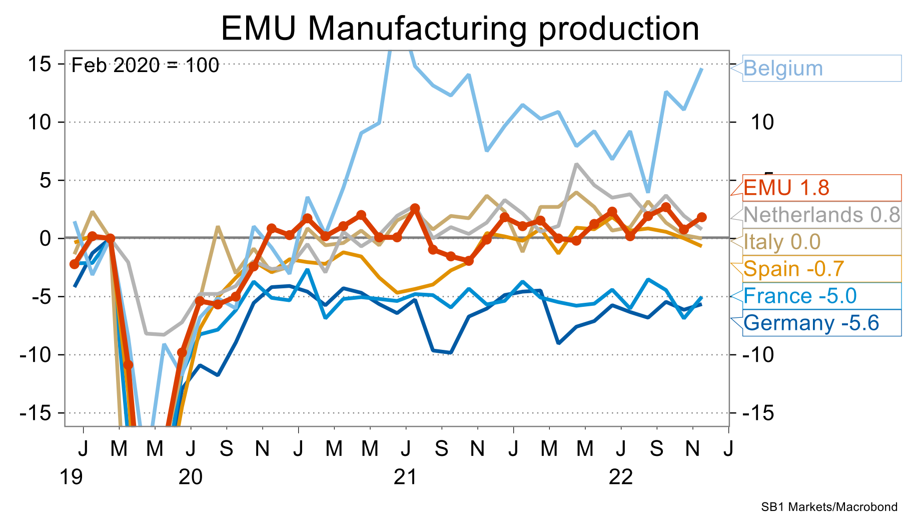


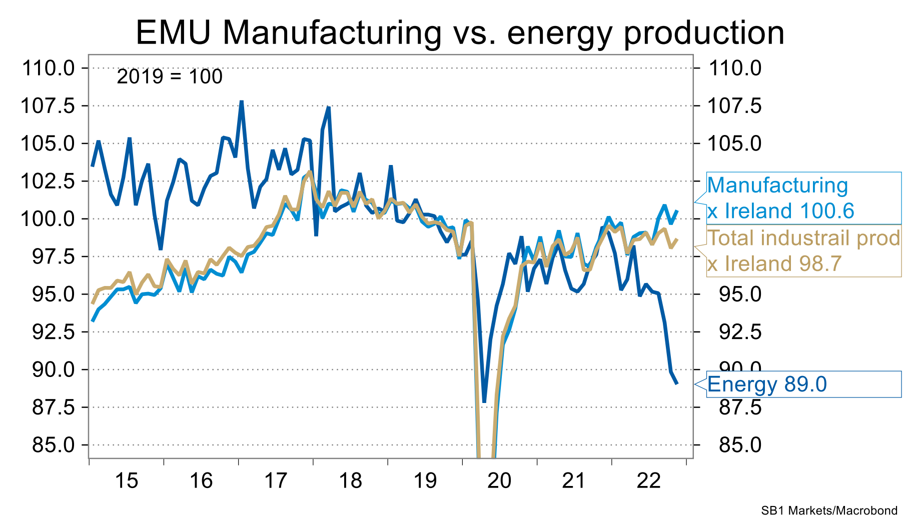


EMU manufacturing production up 0.9% in November, and the trend is OK!

Energy production is falling (10% 'too low') but manufacturing is not that hard hit



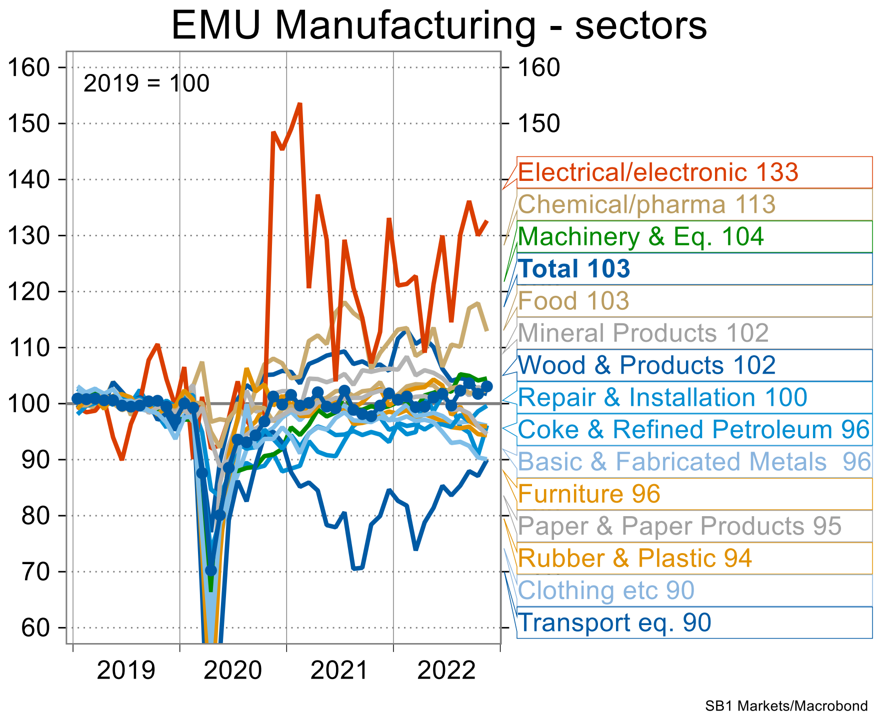


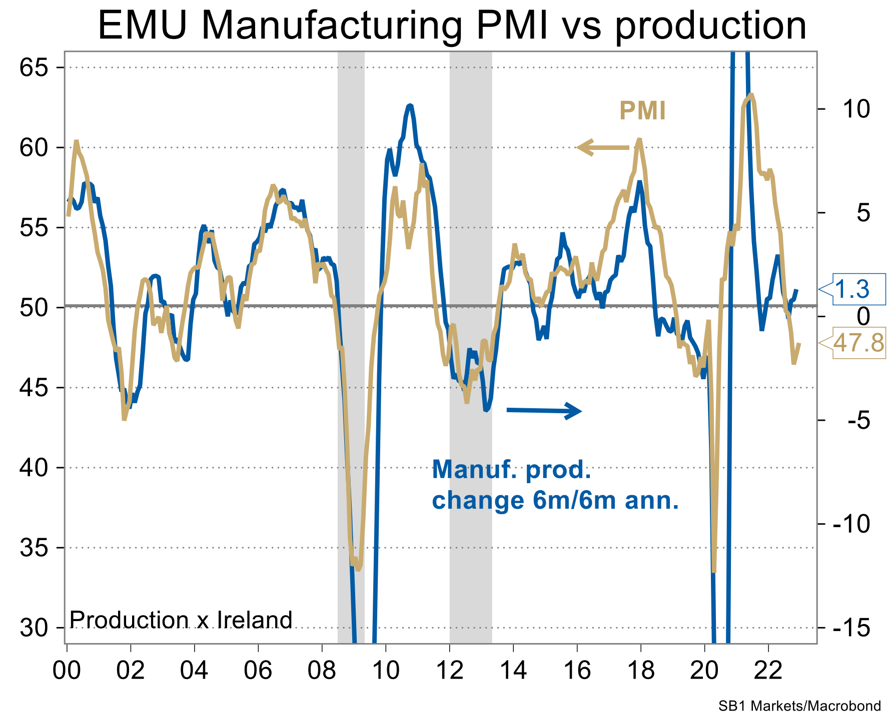


- **Overall industrial production** in EMU gained 1% in November, twice as much as expected. Ex (volatile) Ireland, production rose by 0.6%, which is a more relevant figure
- **Manufacturing production** x Ireland rose by 0.9%, and the short term trend is clearly up (3m/3m + 5.1%!), way better than we expected some few months ago. The energy crisis has not killed the manufacturing sector, at least not so far. Production rose most places
- **The short-term outlook:** Several surveys are weak – but they have stablised, and some surveys are still signalling growth

Many manufacturing sectors still report growth, and none are collapsing

Even if there is an energy crisis. However, surveys are not that bright – a decline in manufacturing is rather likely

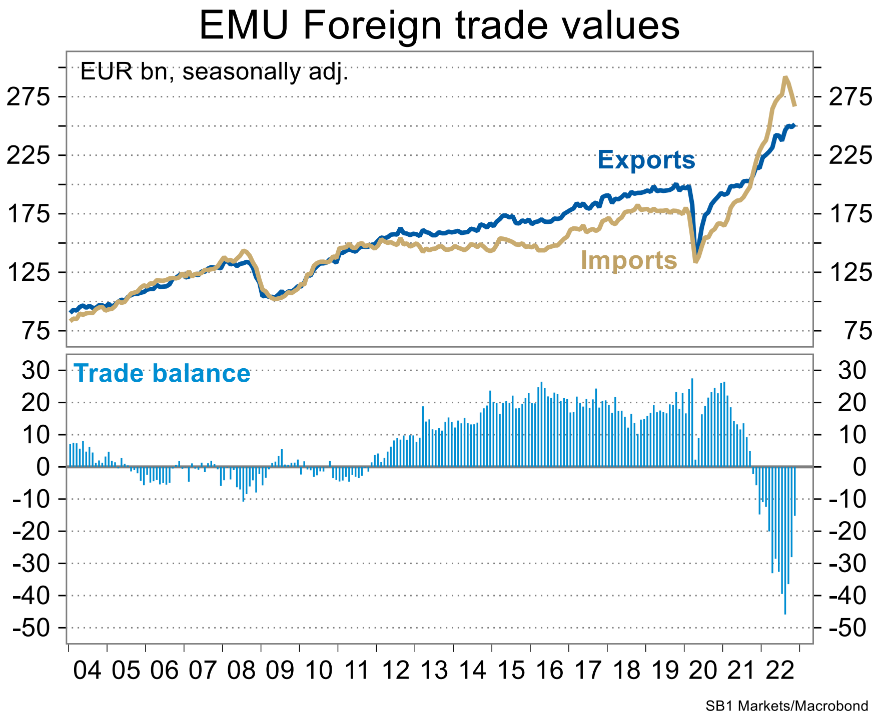


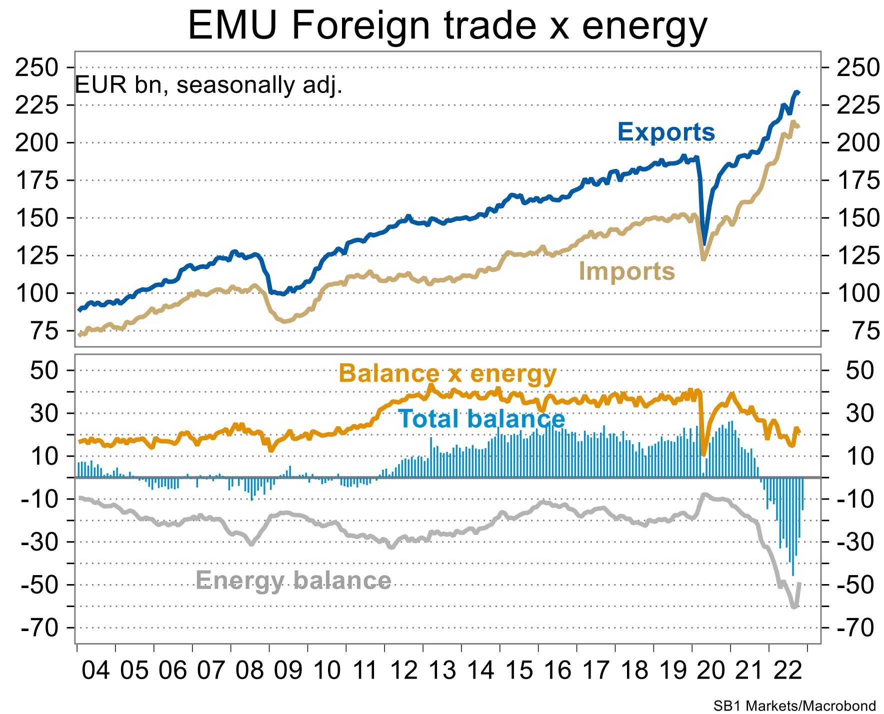


- Transport equipment is still a drag on production – but gradually less so (-30% a year ago, 10% now)
- Metals are down but not more than 4% vs. the 2019 level
- Basic Metals are below par but not by much – even if energy costs have soared. Chemicals are still strong

The trade deficit sharply down – due to cheaper energy imports

.. And a lower import volume. The overall deficit equals 1.4% of GDP, down from 4.1% in August!

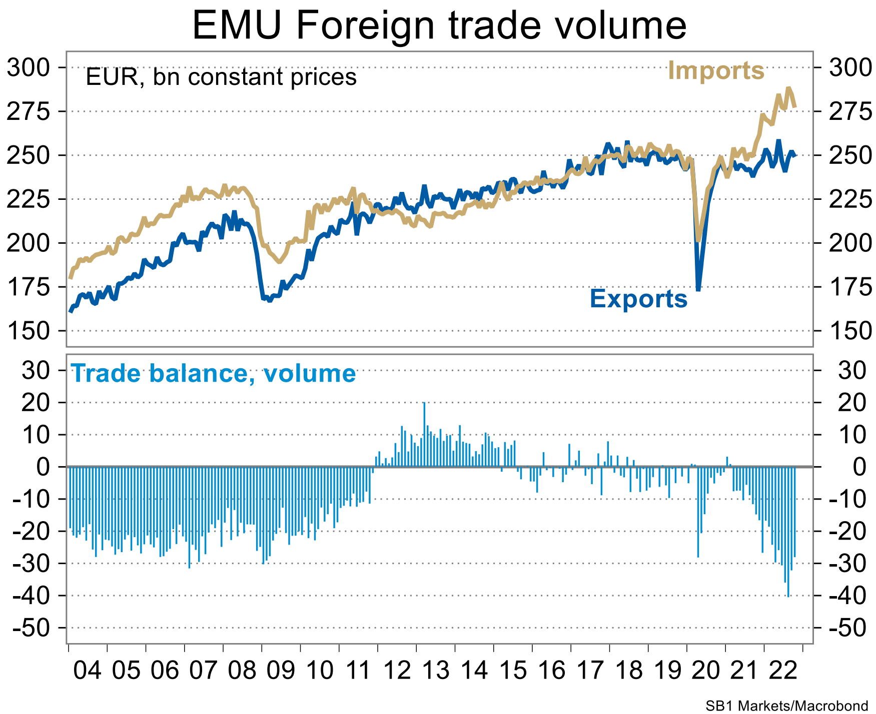




- The **trade deficit** narrowed in further in November as energy prices fell, to EUR 15 bn (s.a.) from EUR 28 bn in October. The trade deficit equalled 1.4% of GDP
- **Energy imports** fell and the energy deficit was reduced more than the overall , and the non-energy balance weakened slightly – but is at 1.8% of GDP, in plus
- **Imports a**re up 21% y/y, while exports are up just 17%. In volume terms, quite another story: exports are close to flat, while imports have soared (but fell in November), check next page

Imports have been rising rapidly, in volume terms, exports not

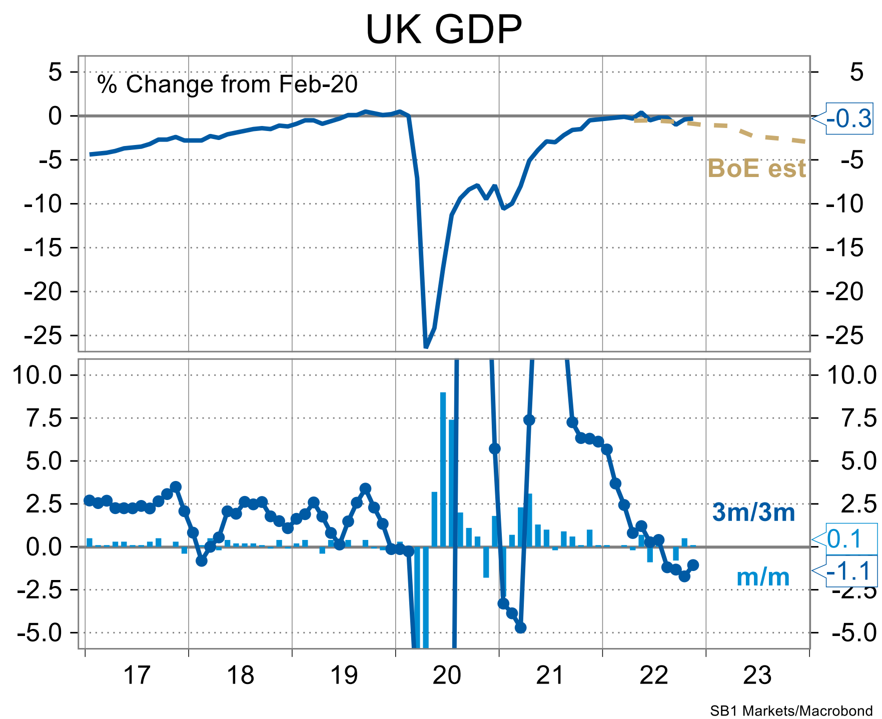
Domestic demand has been strong – and still seems to be

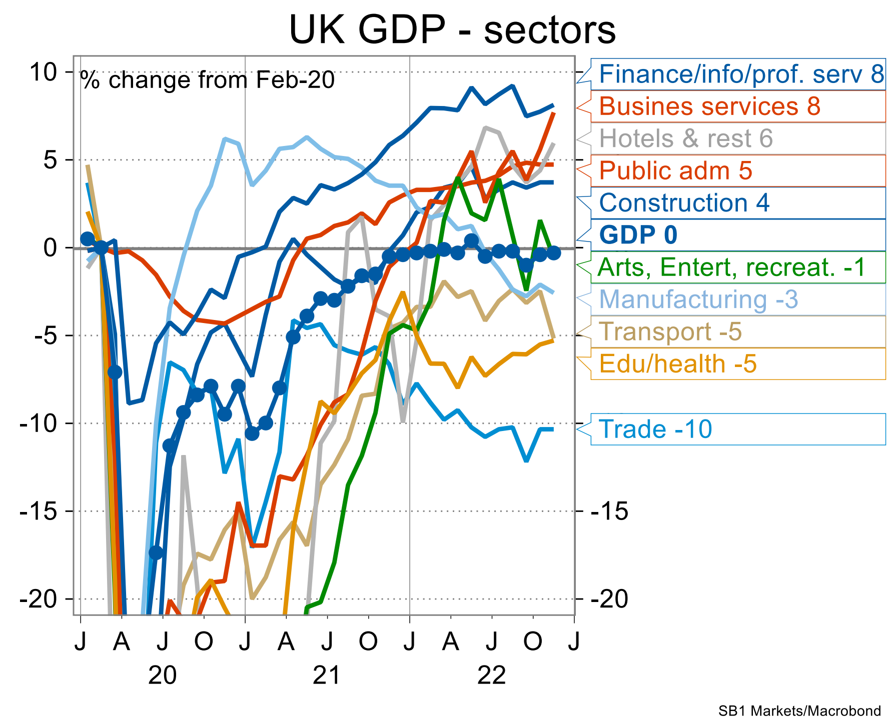


- **Import volumes** are up 10% from before the pandemic – even after a smaller decline past two months, as domestic demand has been strong
- **Export volumes** are close to flat the pre-pandemic level

GDP surprised to the upside for the 2nd month – up 0.1% in November…

…expected down 0.3%. GDP has been trending slightly downwards from the spring, and is down 1.1% 3m/3m

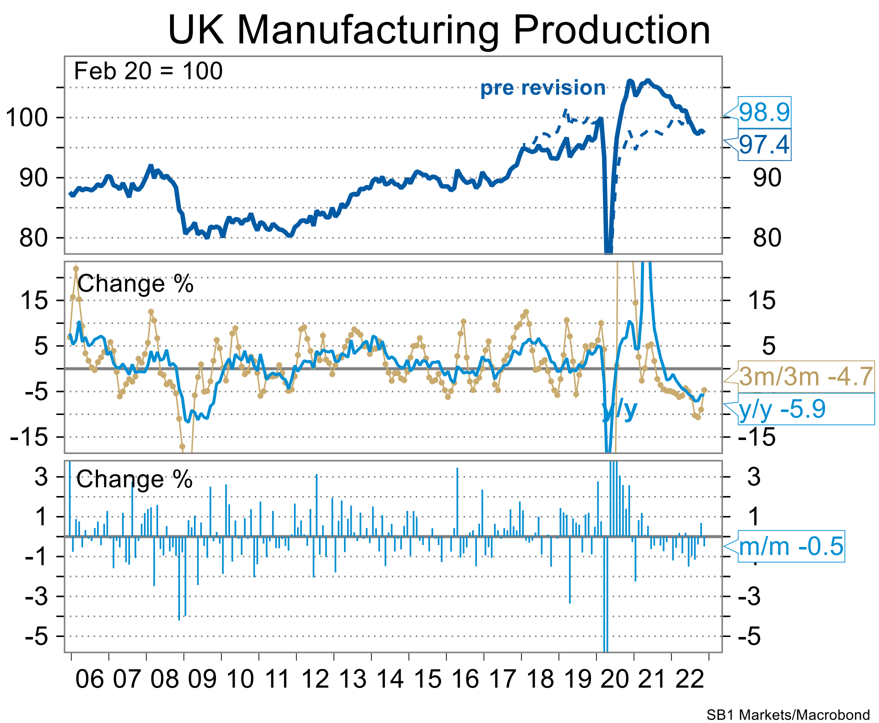


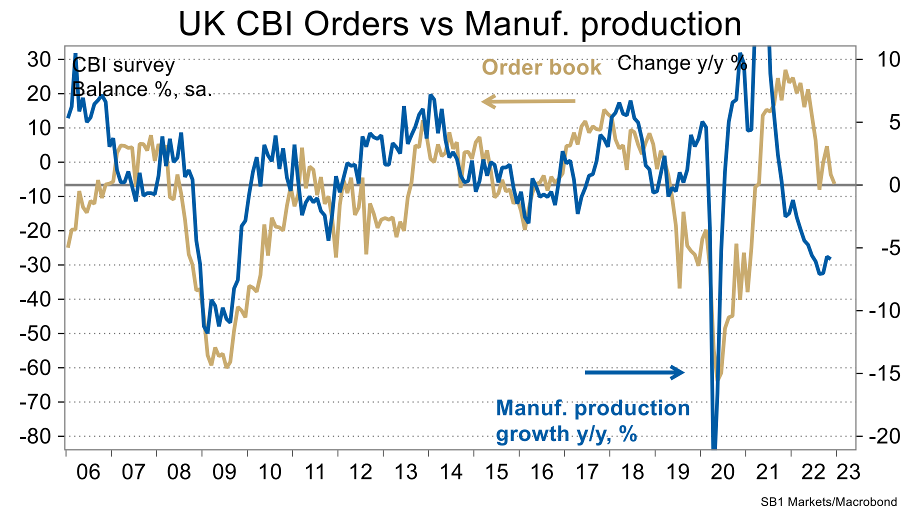


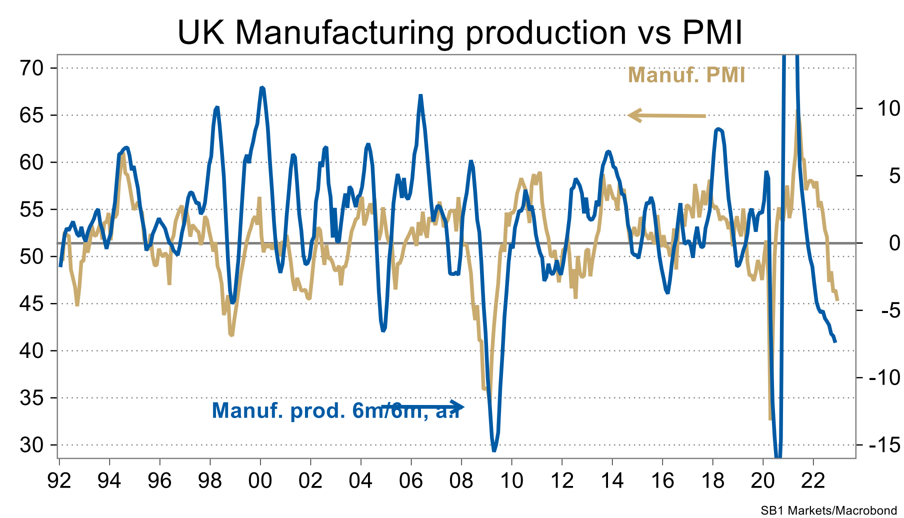
- **GDP** was expected to decline by 0.3%, following the 0.5% increase in October (which was also an upside surprise)
  - **GDP** is at the same level as before the pandemic – that is 3 years without growth. Like in the US the labour supply has contracted somewhat (while it has exploded most other places)
  - **Unemployment** it the lowest in decades, and wage inflation has climbed sharply. Inflation is above 10%, the highest since the early 80s
  - So: Not the best-balanced economy on earth
  - **Bank of England** expect GDP to contract by some well above 2% from the current level through 2023 – and slightly more into 2024. A 0.3% is expected in Q4, so far that does not seem the become the outcome, rather a minor increase
- **Mixed between sectors:** Trade the big loser through 2022, together with manufacturing. Most other sectors are trending up

Manufacturing production down 0.5% in November

Production has flattened past 3 months, but most surveys signal continued downturn



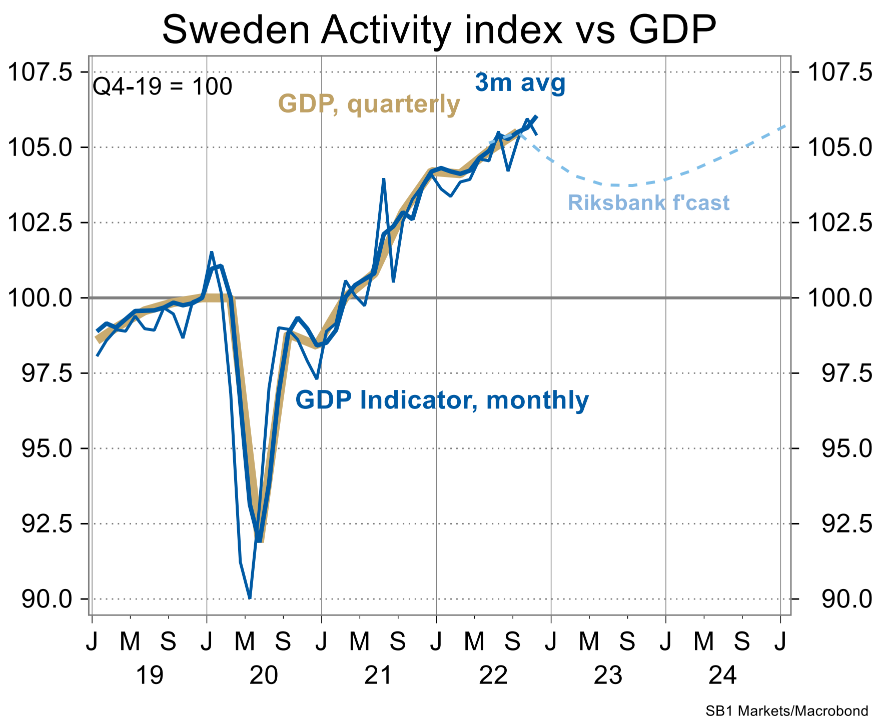


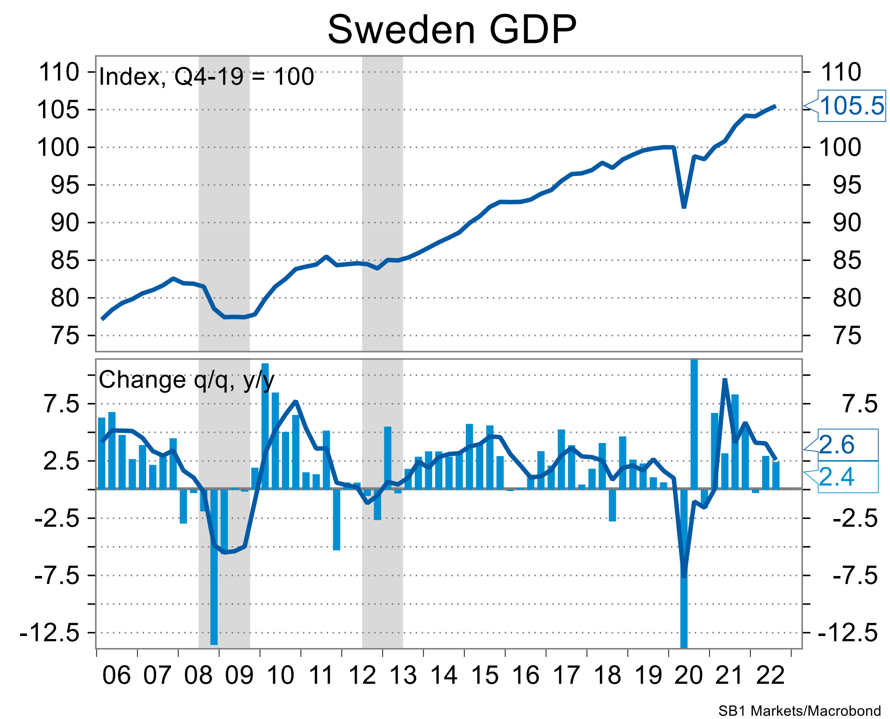


- Production is down 5.9% y/y – and by 4.7% 3m/3m
- Almost all sectors are reporting a downward trend in production
- The CBI survey signals a stabilisation in manuf. orders, while the manufacturing PMI are still heading rapidly downwards

Swedish GDP fell by 0.5% in November, trend is still upwards

Q4 is heading for a far better print than the Riksbank assumed in late November

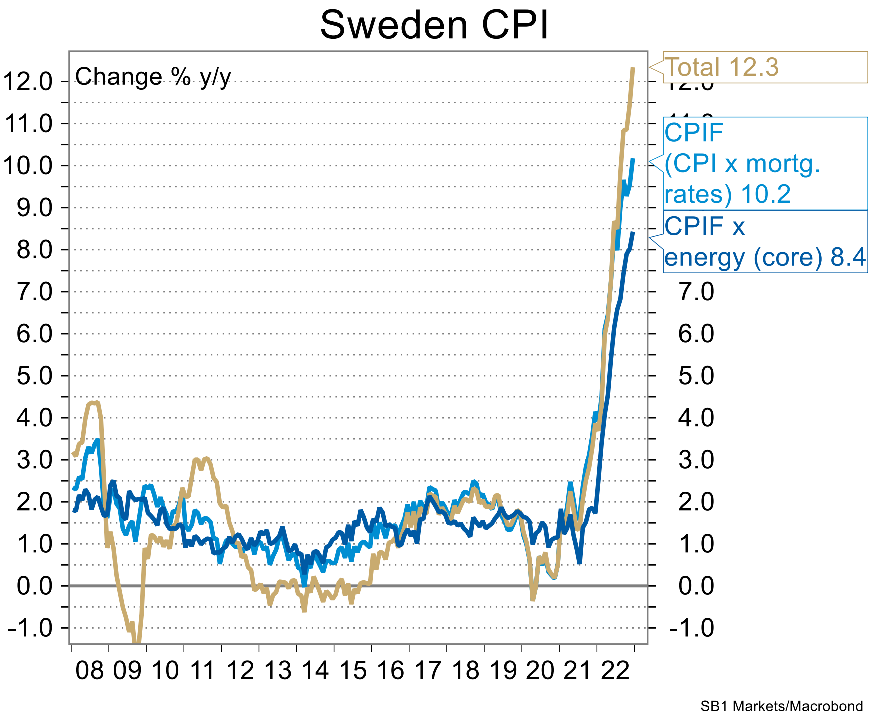


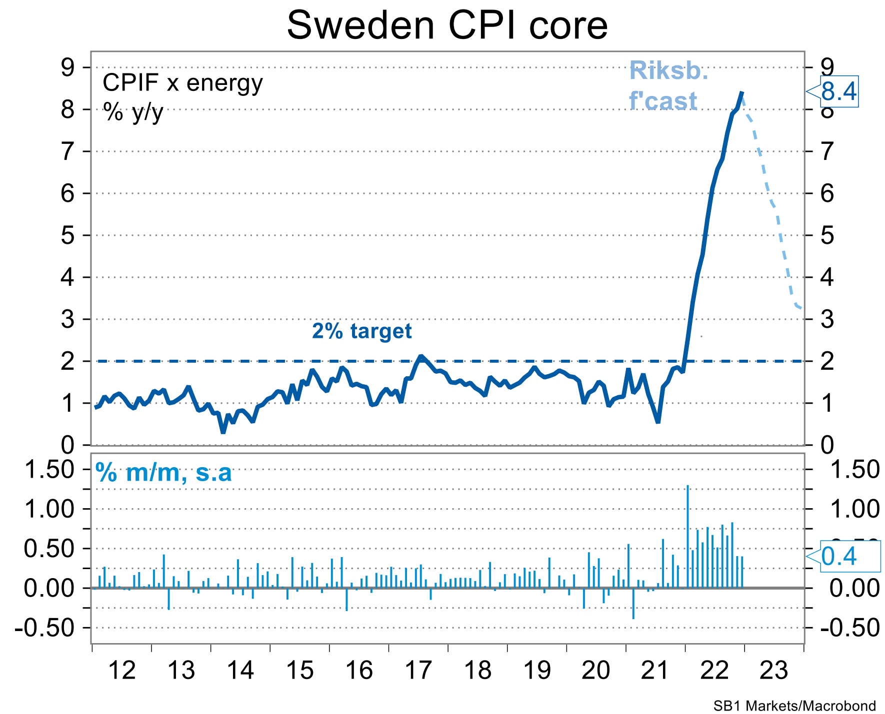


- **December data &** revisions may change the picture, but so far GDP is heading for a 0.6% growth rate in Q4 (2.4% annualised, like in Q3), assuming zero growth in December
- **In late November, the Riksbank meeting** expected a 0.8% decline in Q4 (-3.2% annualised)! In addition, it turned out that Q3 was better than assumed. Not an argument for lowering the banks interest rate path?
- **However, the outlook** is weakening, according to Swedish companies. The KI (NIER) business survey (consumer confidence not included) has fallen to below an average level but is still signalling a slight growth in GDP. The Riksbank assumes a 1.3% decline in GDP to Q2-23 from Q3 last year

Up, up – total CPI inflation up to 12.3%, 0.3 pp higher than expected

Core inflation at 8.4%, 0.1 pp above consensus/Riksbank. The only positive: Core m/m has come down to a 5% pace…

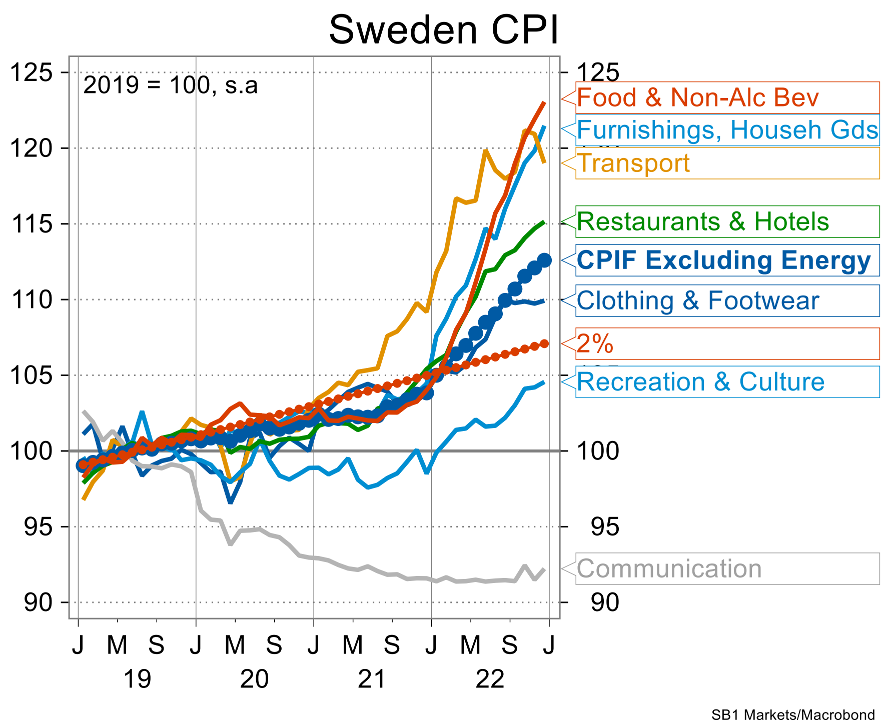


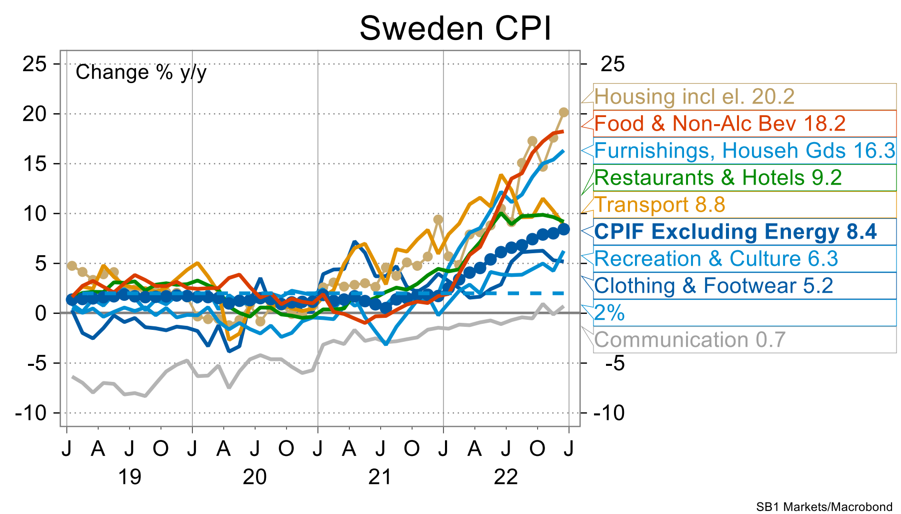


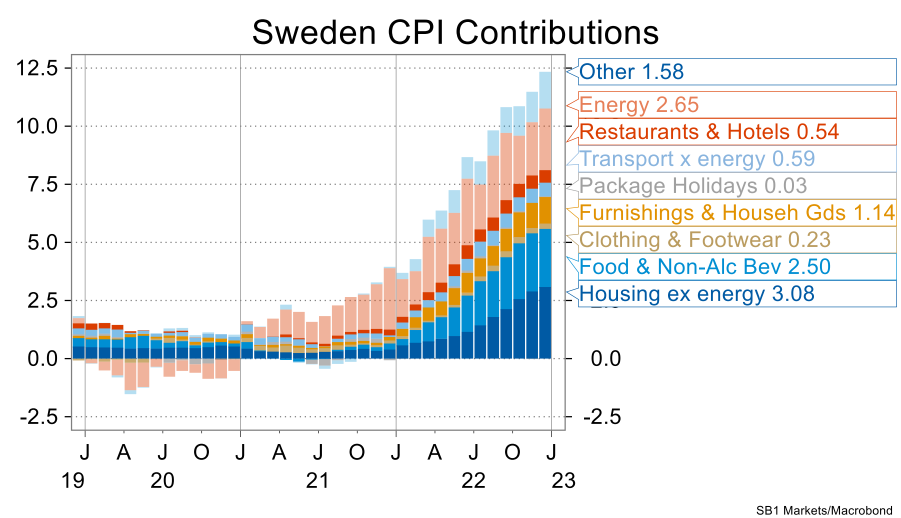
- **CPI-F x energy** (CPI-F is CPI ex mortgage rates), the 'real core', rose 0.4% in December (seas. adj). The core rate has accelerated sharply recent months, to 8.4%. **Food prices** are included in the core, and they are up 18.2% - eighteen point two per cent – y/y, lifting the core more than 3 pp. Thus, the real core is some 5%, more in line with other countries
- **Electricity prices** shot up in December, and are up 41 y/y. Including gasoline/diesel, energy prices lifts the CPI by 2.7 pp. In January, the electricity bill will decline substantially
- Besides mortgage rates, food & energy, several sectors contribute to the unusual lofty CPI print, like furnishings & household goods and hotels/restaurants
- Most likely, the December will turn out to be the peak for annual inflation. Core prices rose by an unprecedented 1.3% in January last year, and that trick can impossible (?) not be repeated now (the Riksbank assumes 0.9%), and electricity prices will most likely decline
- **The market expects the Riksbank to hike the signal rate to almost 3.5%, from the current 2.50% rate**

Inflation in Sweden: a broad acceleration

Just communication is below 2% y/y (like in Norway), and is together with recr./culture, below a 2% path since 2019



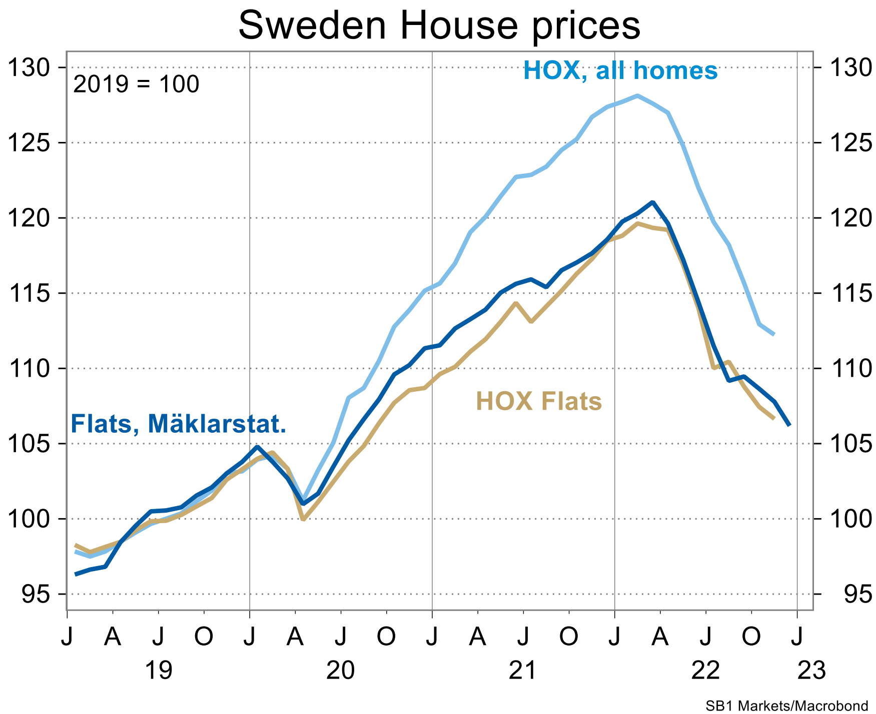


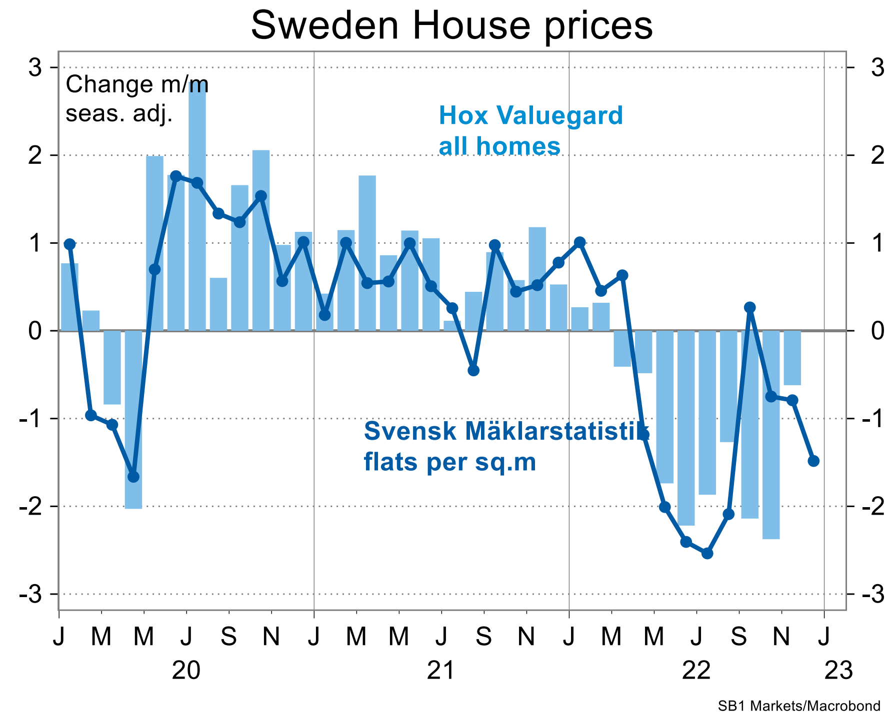


- 2.1 pp of the 3.1 pp contribution from housing in the CPI is due to higher mortgage rates, which are included in the Swedish CPI. Actual rents are up just 5% y/y
- Energy prices lift the inflation rate by 2.7 pp
- Food prices contribute by 2.5%
- All measures of breadth, median, trimmed inflation yields 7% – 10%

Well, the direction is still down, realtors report a 1.5% house price cut in Dec

In addition, November var revised to -0.8% from 0.%. Flat prices are down 12% from the ATH last March

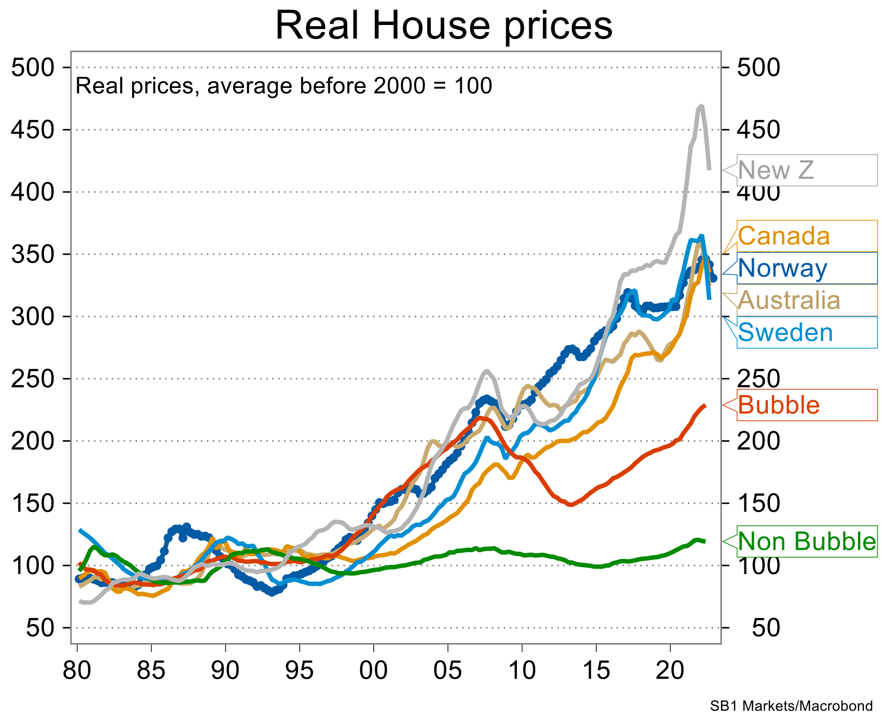


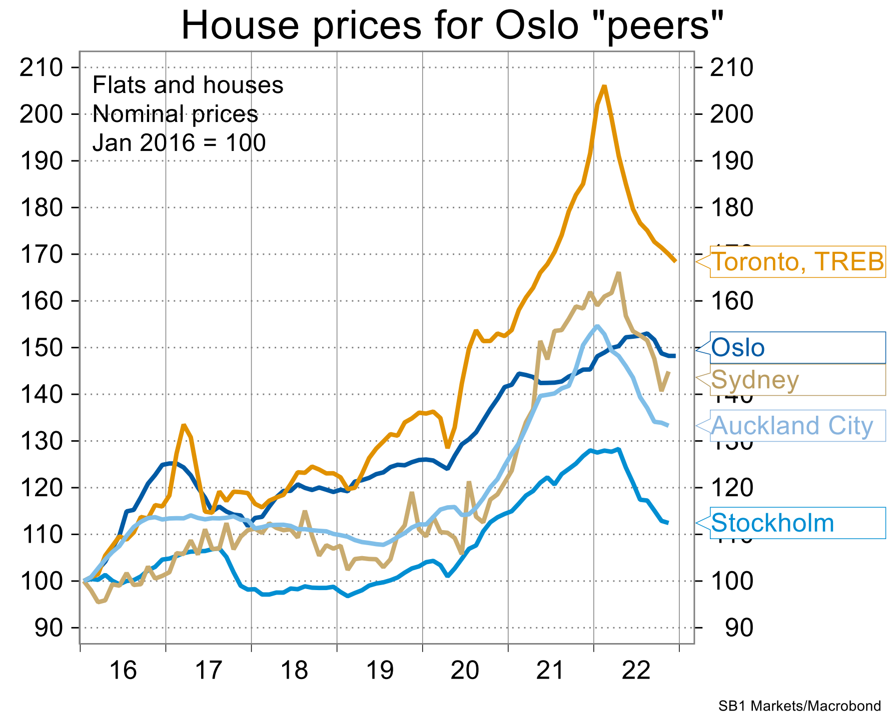


- The HOX index reported a 0.7% fall in apartment prices in November, while single-homes were down 0.8%

Prices are falling in the ‘supercyclical’ capitals, now even in Oslo

Prices have peaked in cities comparable to Oslo - and we believe we have passed the peak here too





- Real house prices are at high levels in both Australia, Canada, Norway, and Sweden – and even more in New Zealand
- Now, prices are falling sharply (where data are updated). Prices in the capitals have turned down in all these countries

Highlights

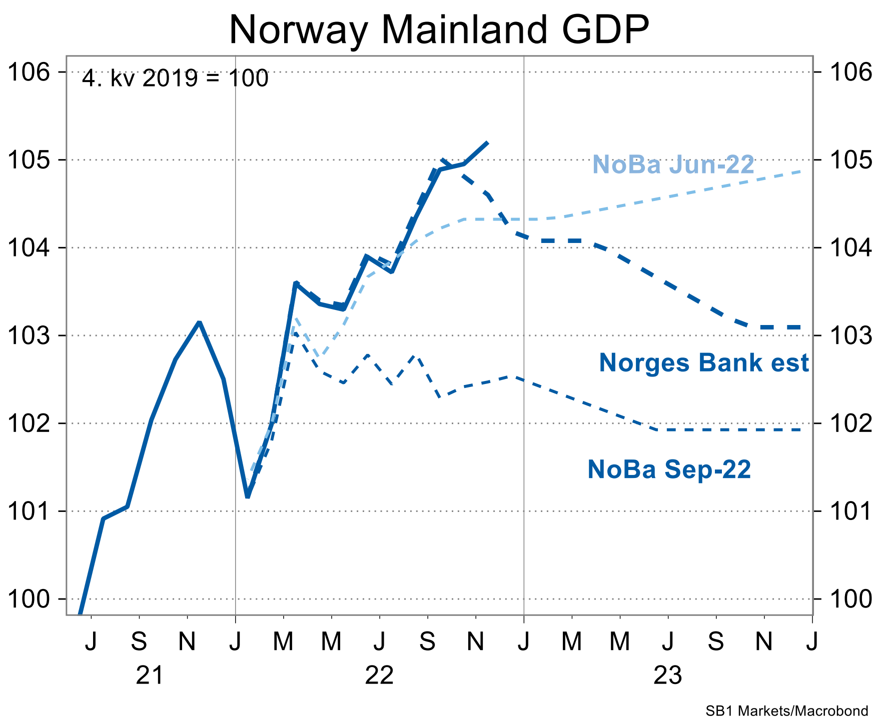
The world around us

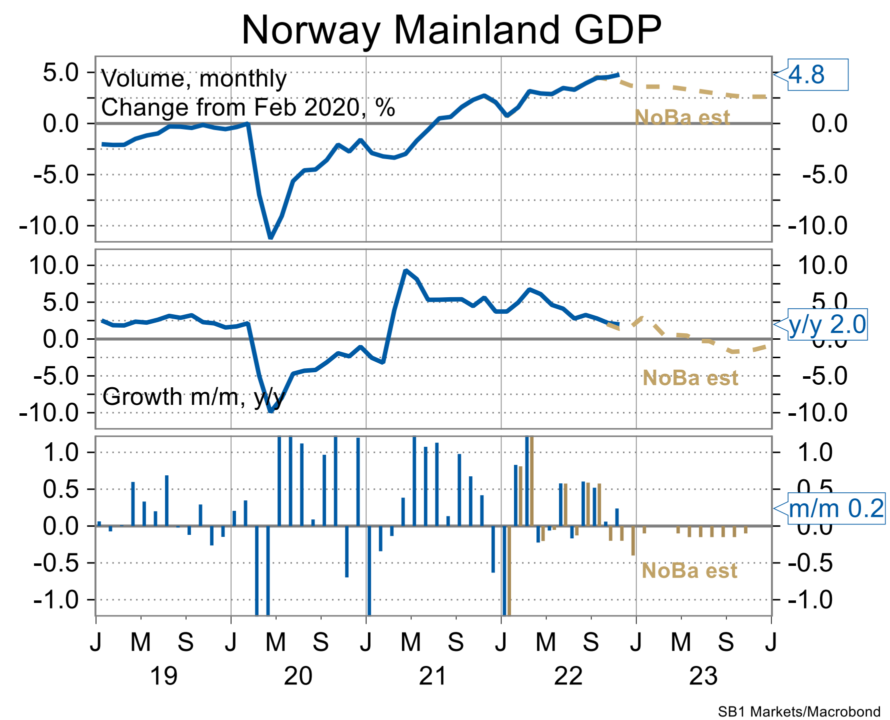
The Norwegian economy

Market charts & comments

GDP up 0.2% in November, in line with expectations, and far above NoBa path

It won't back down: Oct revised up by 0.1 pp – and Nov GDP 0.6% higher than NoBa assumed in Dec

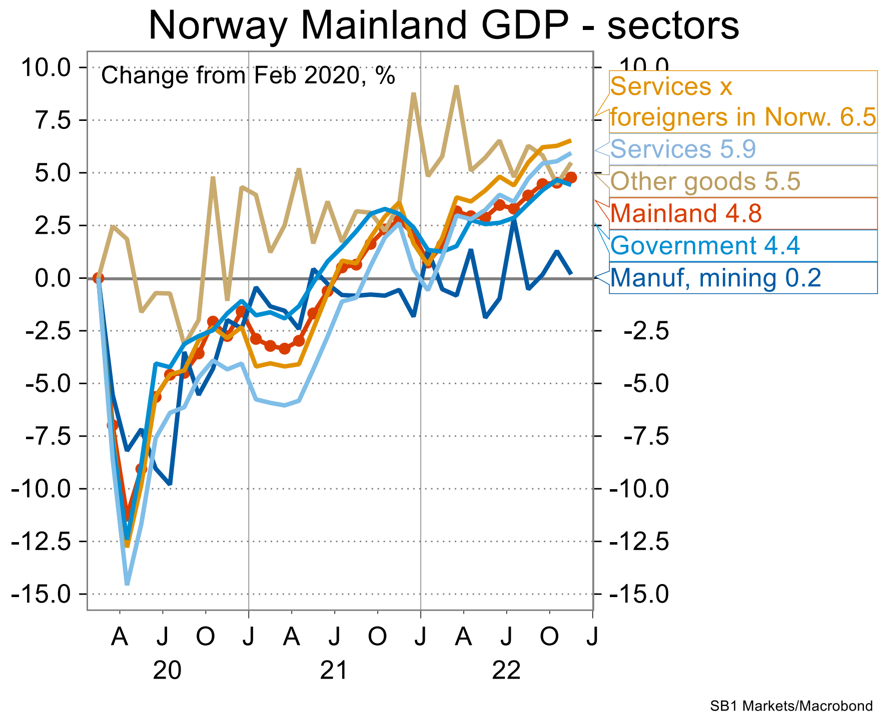


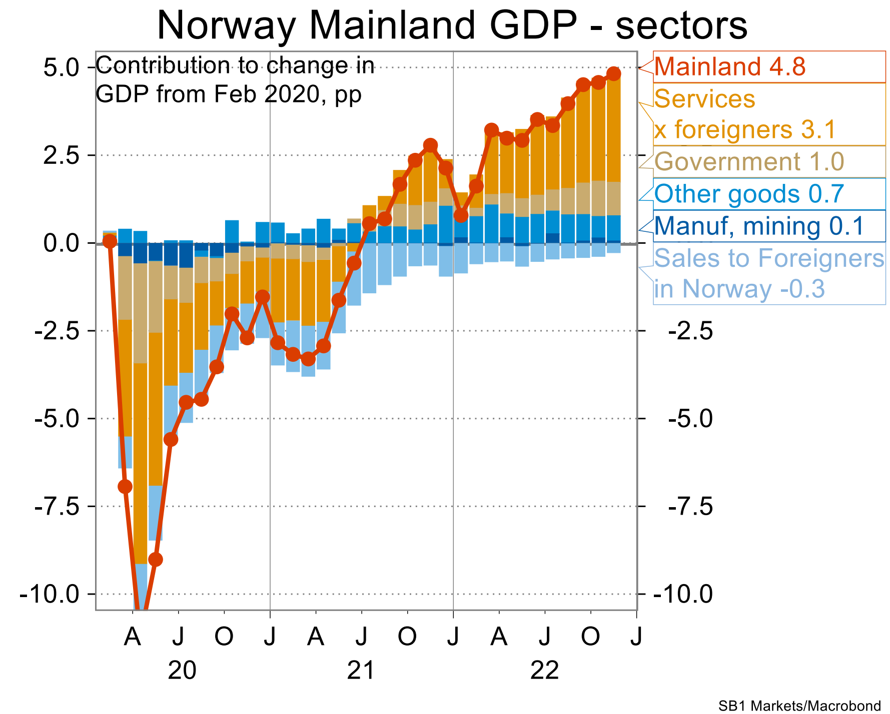


- **Mainland GDP** grew by 0.2% in November, consensus f'cast was 0.2% – 0.4% (our f'cast as the highest), while NoBa expected a 0.2% <u>decline</u>. Growth m/m in October was revised up by 0.1 pp to 0.1%.
- **Production:** Fisheries, electricity production and activity in domestic trade (car dealers were working 7/24 to deliver cars before 31/12) on the upside, manufacturing production on the downside (and more than the manufacturing production index signalled. Government value added fell by 0.1% (which explained 0.1 pp of the difference between our f'cast and the outcome)
- **Demand:** Housing and oil investments fell (we expected an uptick in oil), while ML business investments were up, but less than we assumed. Private consumption rose, broad based – but services less than we assumed. Exports fell
- **What to make out of this?** Once again, GDP has been stronger than NoBa anticipated. By itself not at argument for become more anxious regarding a 25 bp hike in the signal rate in March, which so far has been the Bank's plan

Production: Fish farming & fishery, el. production strongest sectors in Nov

Manufacturing declined by 1.1% in November and is still the weakest sector since before the pandemic

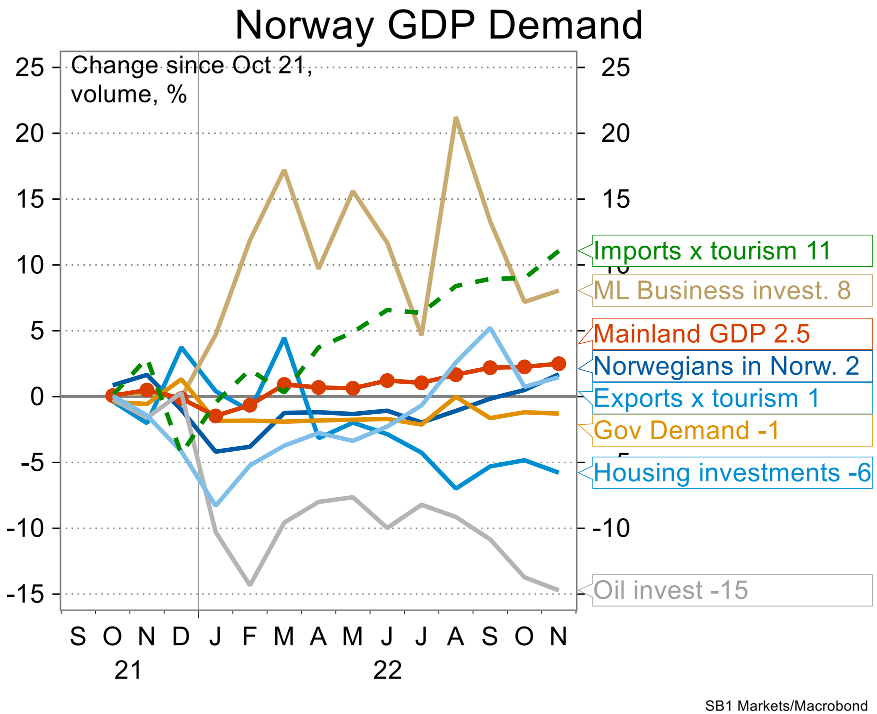


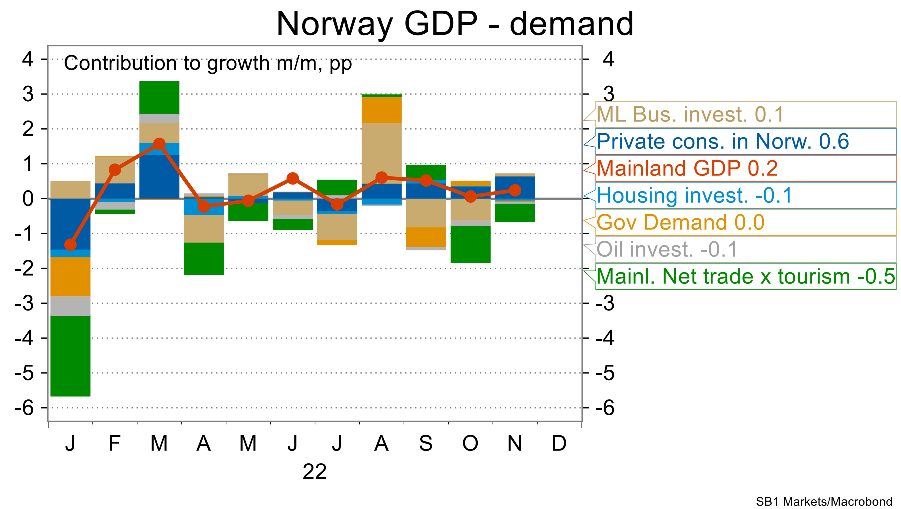


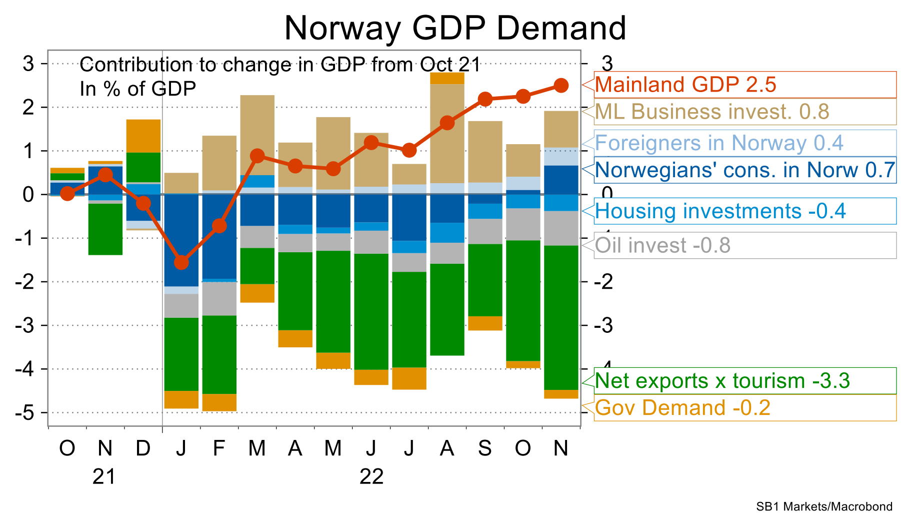
- The ‘other goods’ sector includes among other sectors fish-farming, fisheries and construction

Demand: Oil, housing investments and gov't demand were down in Nov

…while Mainland business investments were up 0.2% m/m and private consumption grew 1.2%



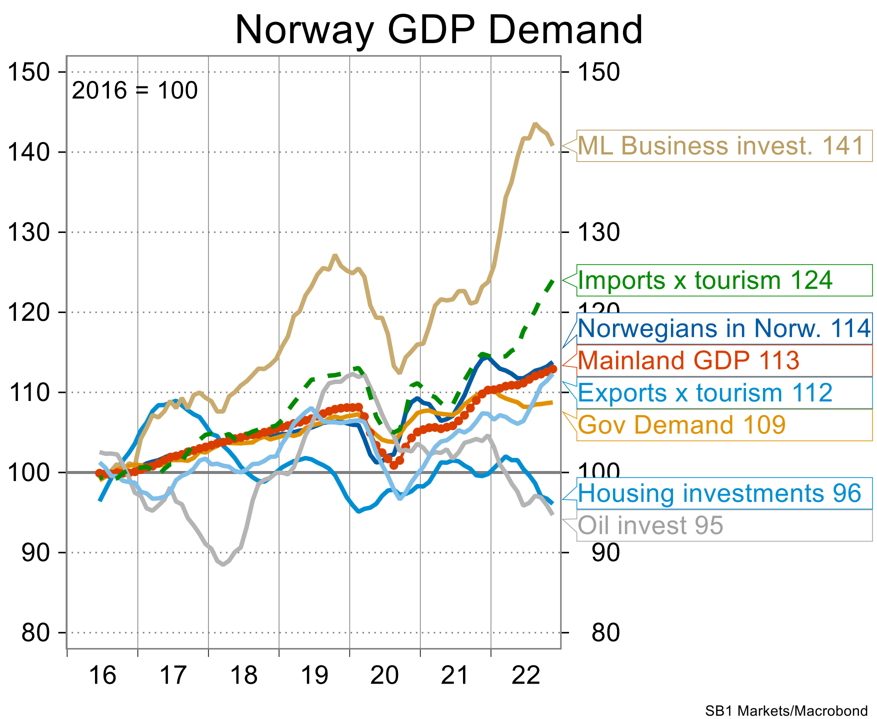




- Oil investments declined by 1.1%, housing -1.0%
- In addition, a 0.1% growth in inventories contributed on the upside

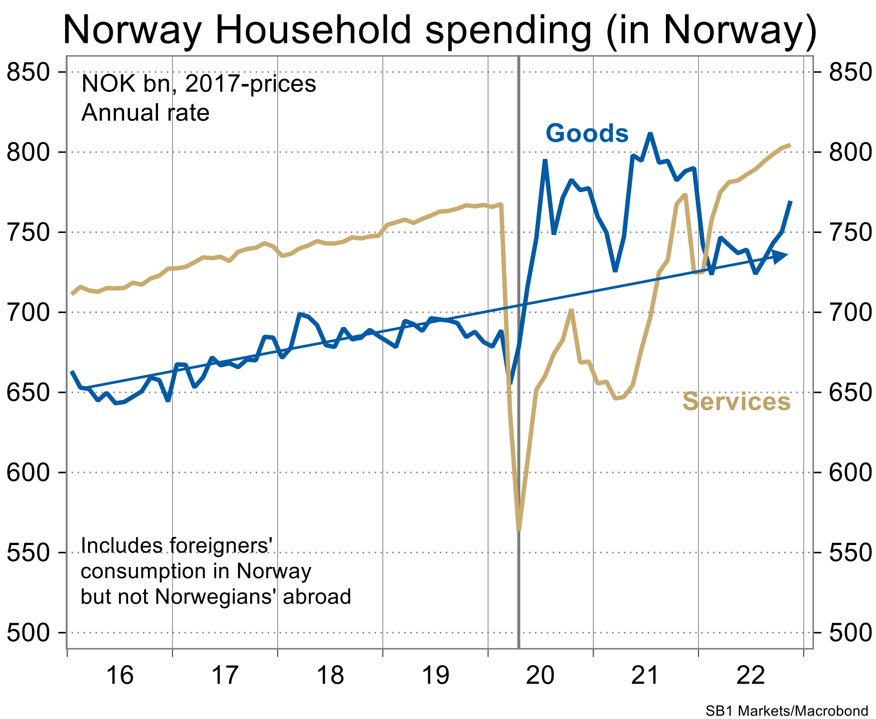
Mainland business investments may be exposed

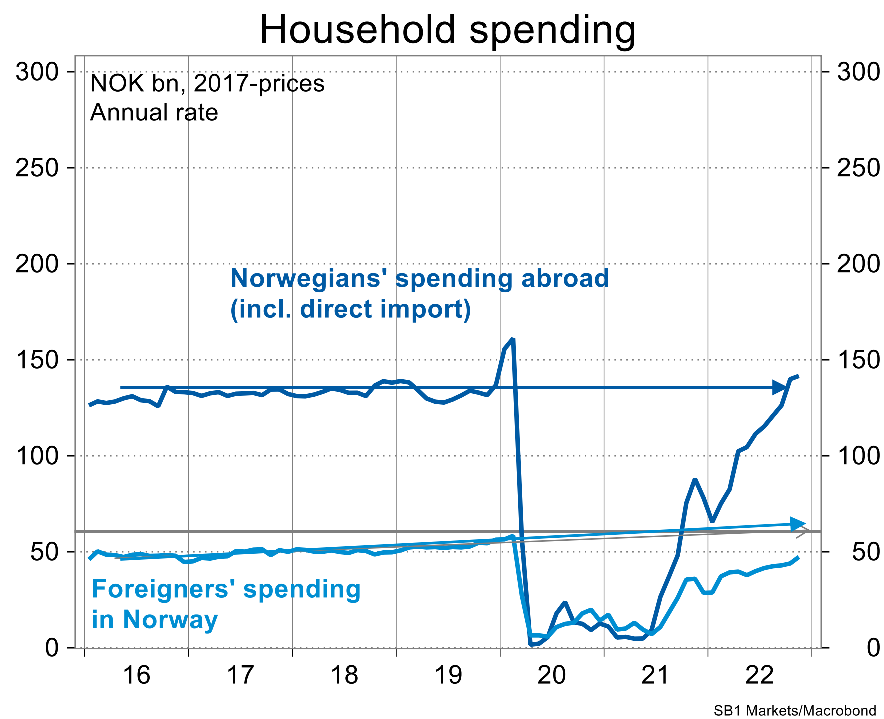
Housing and oil investments on the downside. Oil investments will very likey soon turn up. Housing probably not



Services consumption in Norway has fully recovered to the pre-pand. trend

And consumption of goods is well above, due to the sharp increase in auto sales. Spending abroad at the p-p level

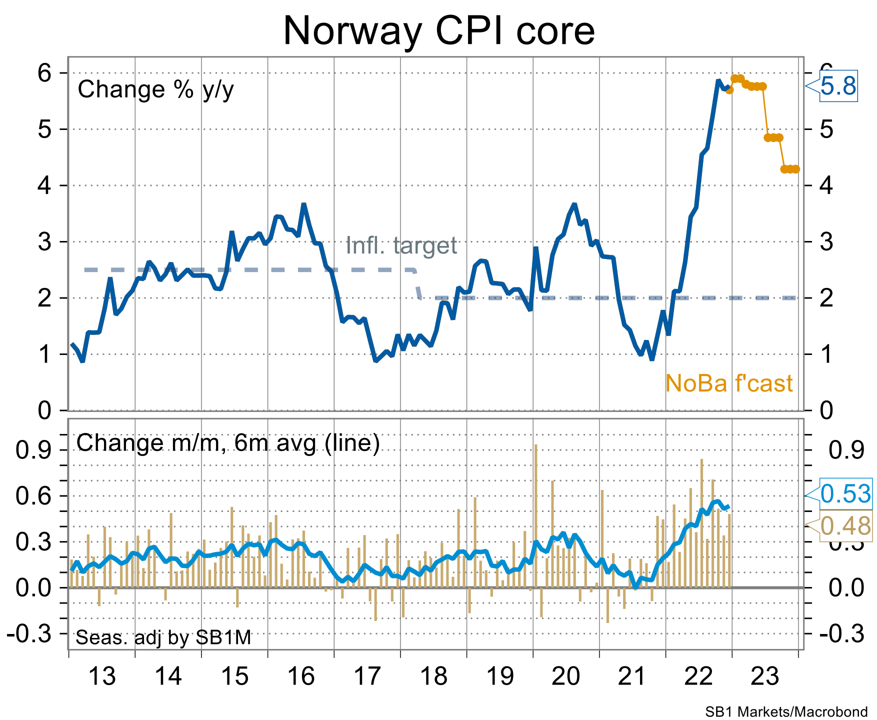




- Foreigners’ spending in Norway is recovering but remains roughly 20% below the pre-pandemic growth path
- Even if foreigners are spending less, total spending on services in Norway is back on track. Somebody else must be spending more…

Headline inflation lower and below consensus in Dec, but the core was higher

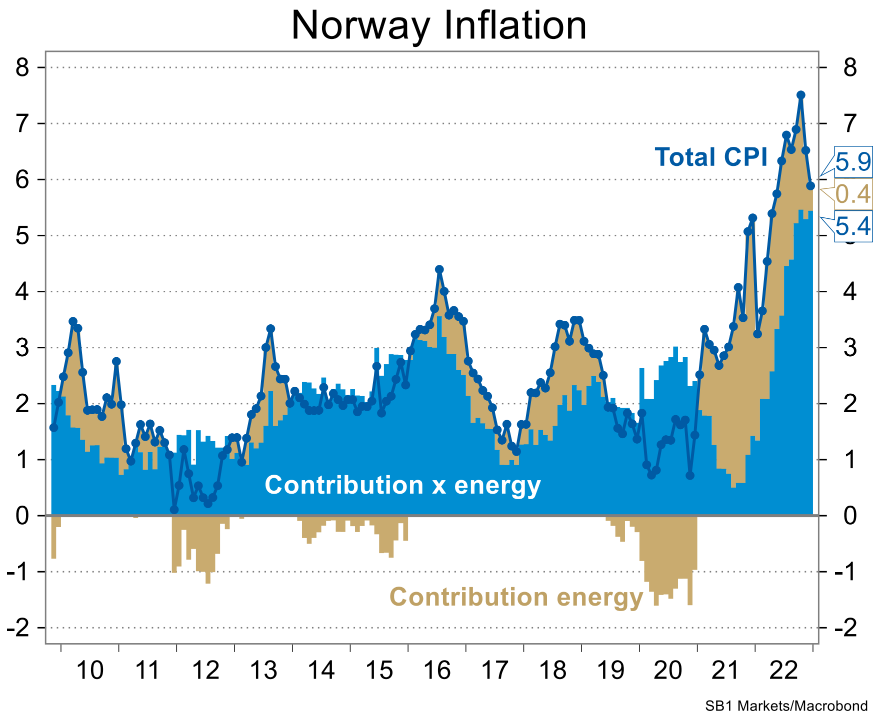
The core index 0.1 pp to 5.8%, consensus & NoBa at 5.7%. 58% of the CPI components are up more than 5%



- The **headline CPI** slowed to 5.9%, from 6.5%, as we expected. Consensus was at 6.1%, and NoBa at 6.0%. The decline was greeted as good news (and lower inflation is) but the details were not favourable:
- **CPI-ATE** (ex. energy and taxes) rose 0.5% m/m (s.a) in Dec (we expected 0.3%), and the annual rate fell accelerated 0.1 pp to 5.8% we expected 5.5%, consensus & NoBa expected 5.7%
  - **What lifted the core**: PC/TVs, cell phones & textiles, all imported goods. However, of the past year, the lions share of the 5.8% rate of inflation is due to domestically produced goods and services (influenced by imported goods prices and energy, we guess)
  - **Imported prices** are up 6.4% y/y, domestically produced goods/services 5.8%
  - **Food prices** were flat m/m but are still up 11.8%, though just 5% above 'trend'. Prices were very low a year ago
  - **The median/underlying inflation** rate is close to the annual core rate, at 5.5% – 6%. The 6 m underlying core rate is at 6.5%
- **Energy prices** fell – and a tad more than even we expected. The **electricity index** fell 3.4% (we expected flat) even if spot prices rose 2% (due to semi-fixed contracts), while **gasoline** prices fell by 8.8% (we expected -5%)
- **The outlook**
  - **Market electricity prices** have fallen sharply recent weeks, and so will the electricity CPI component – but probably not in January (semi-fixed contracts, once more)
  - **Gasoline prices** have come down to a 'right' level, given oil/product prices – possibly no further downside (m/m), but the annual rate will collapse
  - **Core inflation** has not started slowing, but we expect that to happen during H1, due to lower goods prices. Food prices may create problem again, in February

Implications for Norges Bank and the policy rate

This was a bear report, not a bull report, even if the December surprise came from imported goods

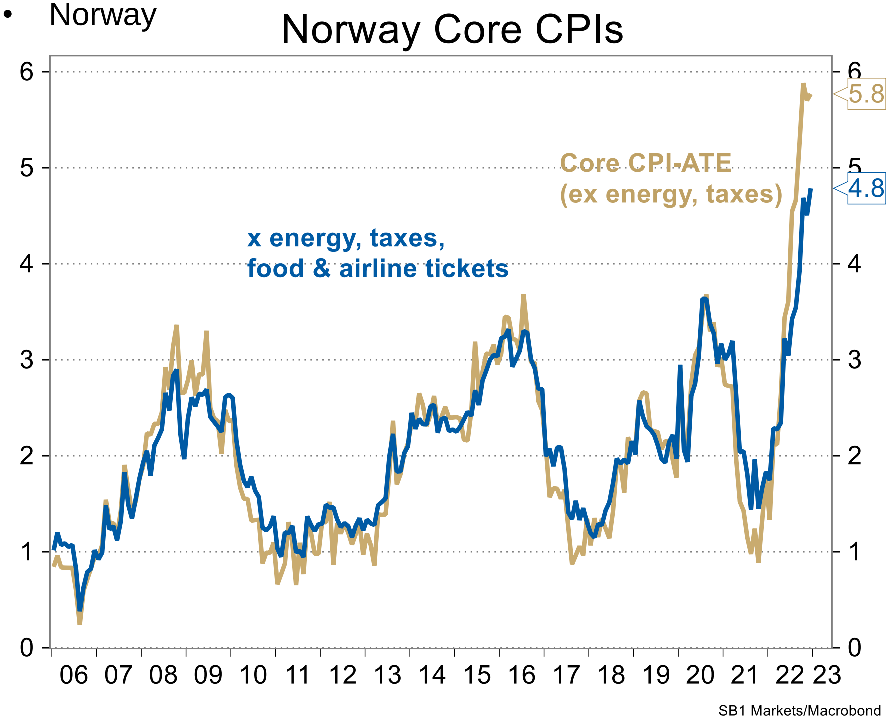


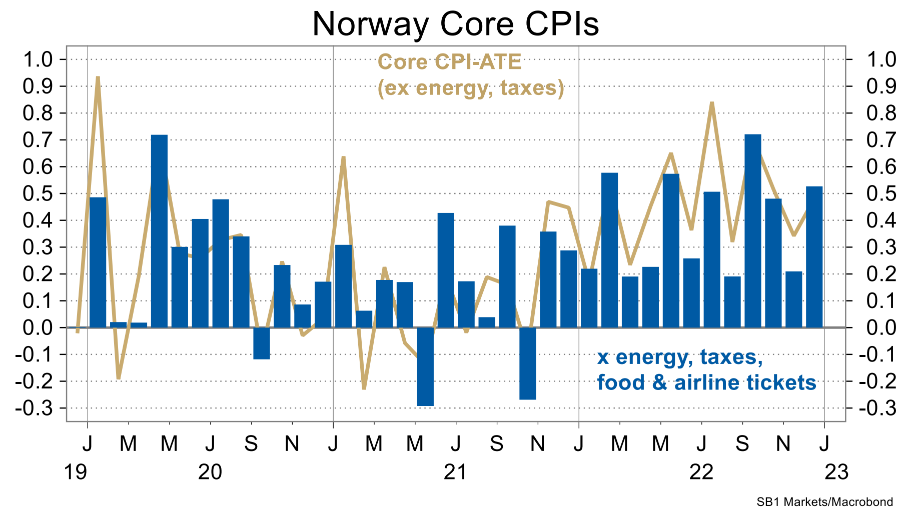
- **Inflation at 5.9%, core at 5.8%, so what?**
  - **Headline inflation** has come down, but the rate is high – and it will probably turn up again in January (before falling in February)
  - **Core inflation** is also very high and higher than expected, and is not yielding – and it is still broadening
  - For **Norges Bank**, as all other central banks, wage inflation is the dominant risk vs inflation over time. So far, wage inflation has not accelerated, as we expected it would. However, as inflation will be high into 2023, there still is a risk that wage inflation will accelerate following the wage negotiations the coming spring, even if the economy is slowing.
  - In December, NoBa signalled another 25 bp hike in Q1 and possibly one more in Q2. This inflation report has not reduced the chance for that second 25 bps hike
  - Last week, markets everywhere were bullish as inflation was coming down

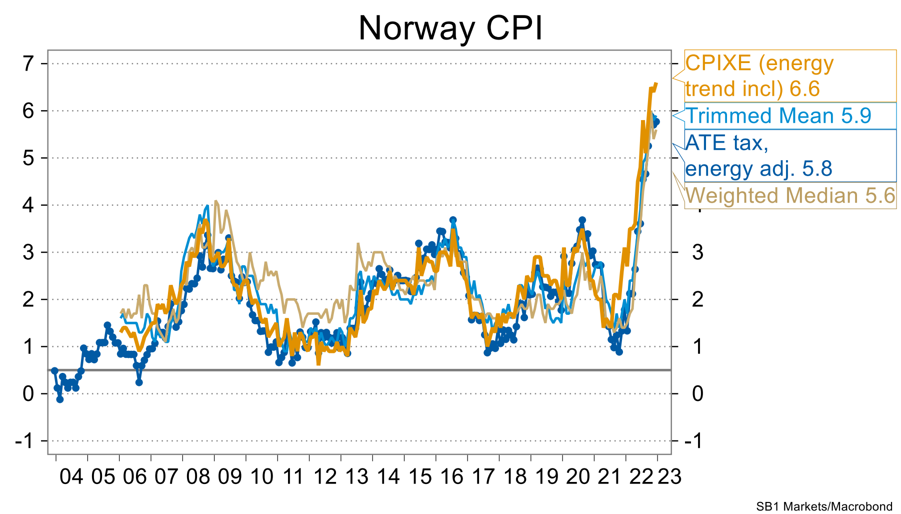
The ‘real’ core (core ex food and airline tickets) inflation up to 4.8%, ATH

In addition, all measures of underlying inflation suggest <u>a 5.5% – 6.5% level</u>

- Norway





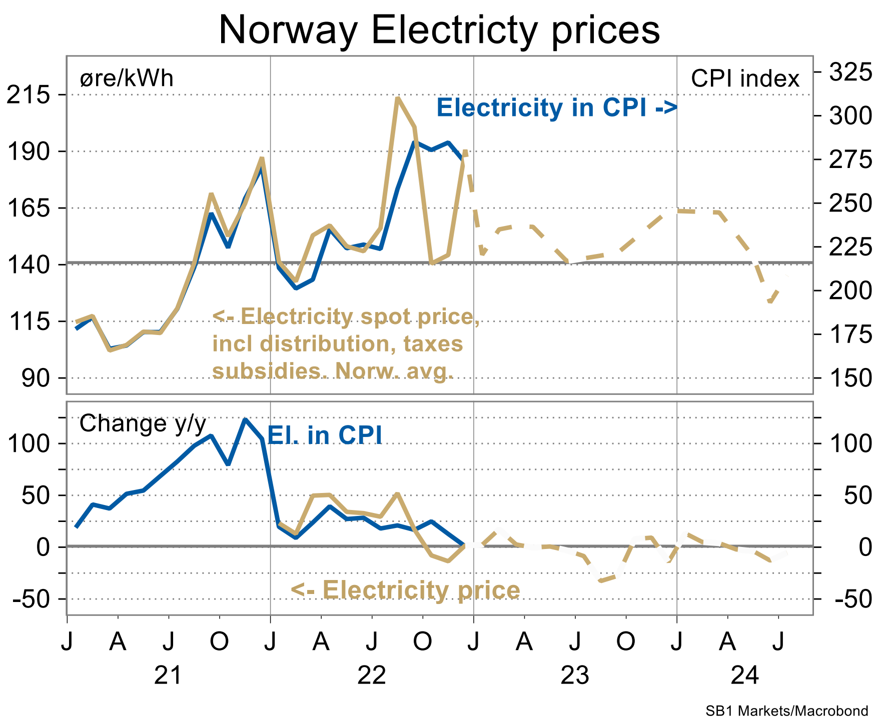


Of the sub-components in the CPI:

- 86% up > 2% (up from 82% last months)
- 57% up > 5% (up from 52%)
- 19% up > 10% (<u>down</u> from 22%)

Finally, we got it approx. right vs. electricity prices in the CPI

The semi-fixed price contracts have created problems recent months, but we are now back on track (until further notice)



- For the rest of the year: From March onwards, current future prices indicate a zero, and negative growth rate, measured y/y

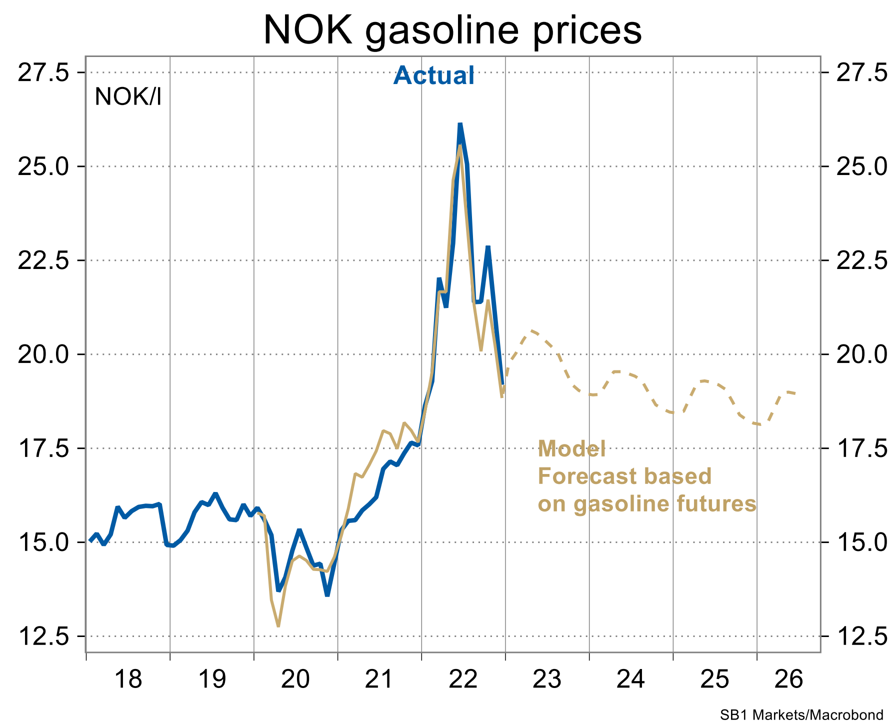
- Even if **spot prices** + transfer fees + taxes – subsidies rose by some 24%, we assumed that the average consumer price (in the CPI) would be unchanged. Why? The **semi-fixed price contracts** (1 m fix) turned out to be cheaper than the spot price based contracts better in line with the spot market, after being miles above in Oct & Nov (where our f'casts were widely off mark)
  - **Dec contracts** for the semi-fixers were based on a Dec future price at some 180 øre/kWh, while the spot turned out to be higher, at 240, and a much larger subsidy was returned to the fixers too. Thus, the semi-fixed contracts yielded a comfortable low energy bill!
- By luck and accident, we were quite correct. SSB reported at 3.7% decline
- **In January**, spot prices have once again, at least so far, fallen sharply. The average is so far 110 øre/kWh – and could end up at 100 – 150 øre/kWh, down from 240 øre in December (avg. so far 110 øre/kWh). If that was the whole story, the CPI index would have fallen some 20% – 30% m/m in January (like prices fell in Jan-22)
- However, in mid December, the semi-fixed contract prices were set based on a **January future price** around 310 øre/kWh. The **subsidy** will be limited (since it is based on the spot price which probably will be low) and the bill in January will be higher than in December for these fixers (if there are anybody left on such contracts now). That is, even if the spot price has 'collapsed' just like in October and November
  - The semi-fixed contracts have probably deemed to be less attractive recent months, and the market share of some 17% before the autumn, may now be lower. Still, as their price deviates grossly from prices on contracts based on spot prices, they have a sizeable impact on the average household price, calculated by SSB
- We assume these twists and turns will be cancelled out in February. <u>But the January CPI print will quite likely be lifted due to these technicalities. As prices fell sharply last year, we expect a positive contribution from el. prices to annual CPI growth in January</u>

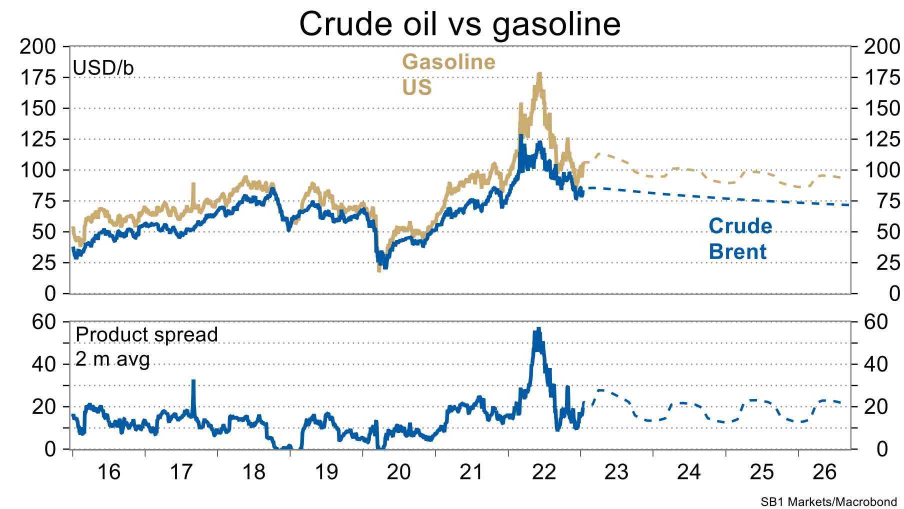
A 90% subusidy efficiency is assumed as more electricity is used when prices are high (due to low temperatures

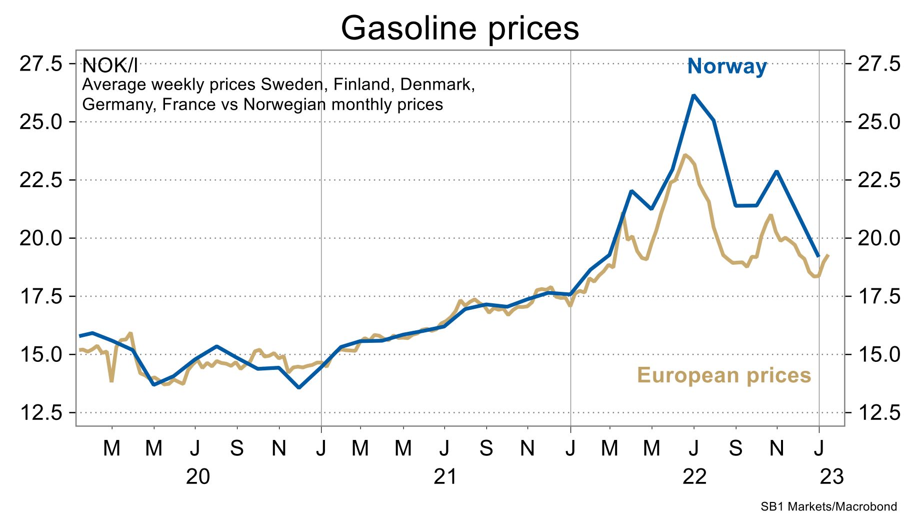
SpareBank 1 MARKETS

Gasoline prices fell further in December, but markets signal that's it for now

Upside risk m/m the coming months but the annual rate will soon turn negative ☺



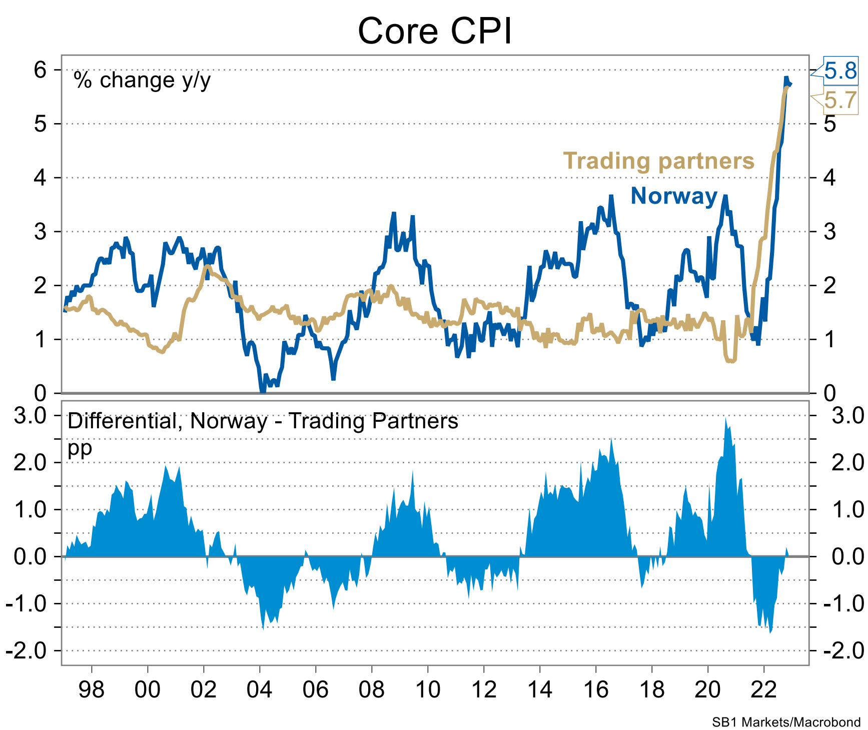


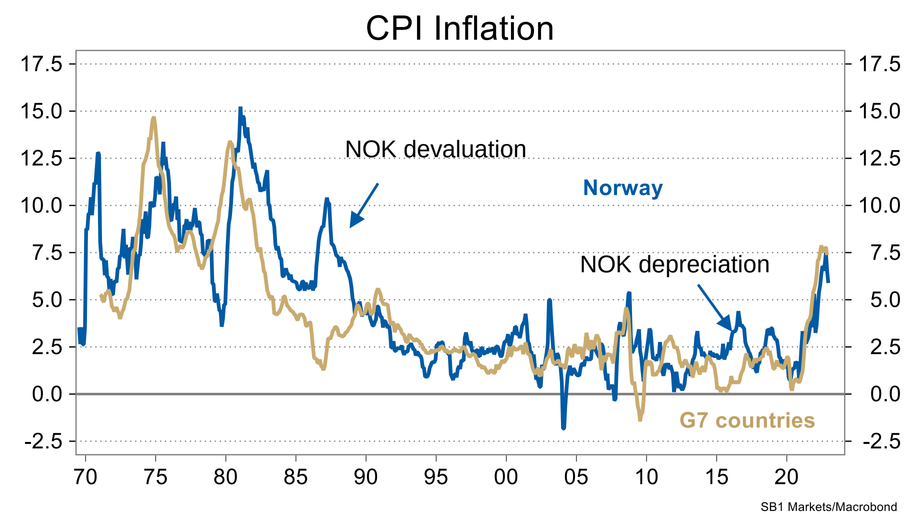


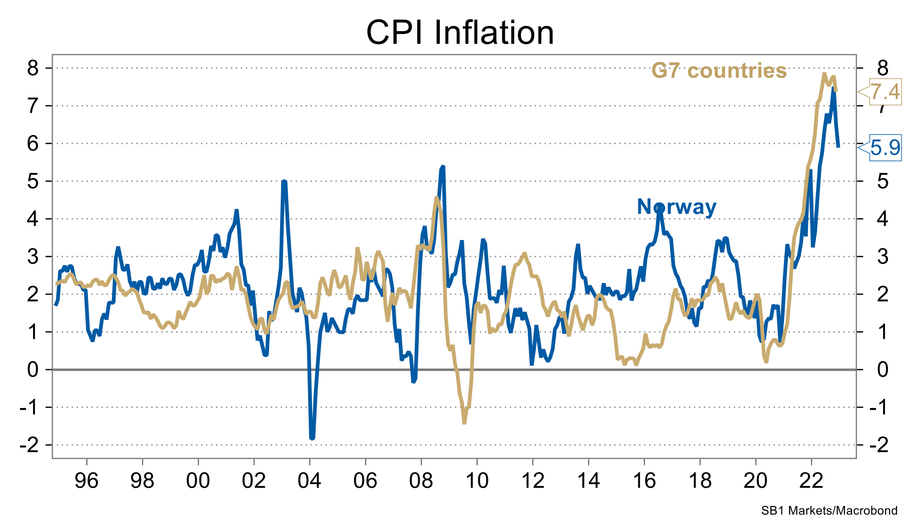
- Refinery/product margins widened in early 2022, but have fallen back to normal level. In the US as well as in Europe, gasoline prices fell until mid September, but turned up again until mid October. Now, prices are falling again

Norway vs ROW: The large, long-term CPI 'regimes' have been correlated

But limited short-term correlation, at least in the 'low-inflation regime'. *In which we are no more*







- Norwegian core CPI vs. trading partners' core has been close to uncorrelated past 20 years. The headline CPIs have been somewhat better correlated, due to co-movements in energy prices
- During the last large inflation cycle '70s and early '80s Norwegian headline inflation was quite closely correlated to the global (G7) CPI cycle (and mostly lagging)

Energy prices surprised to the downside…

But data equipment/TVs, cell phones & telecom services, household textiles lifted the core CPI

		Change m/m, seas. adj			Change y/y			Contribution, pp		
Dec-22	Weight	Out-	SB1M	Dev.	Prev.	Out-	SB1M			Dev. vs
CPI ATE, seas adj.	%	come	f'cast	pp	month	come	f'cast	m/m	y/y	f'cast
Food, non alc bev	12.9	0.2	0.3	-0.1	12.6	11.5	11.4	0.03	1.48	-0.01
Alcohol, tobacco	4.2	0.2	0.3	-0.0	7.3	6.9	7.0	0.01	0.29	-0.00
Clothing, footwear	5.1	-0.4	0.4	-0.7	2.1	1.4	2.3	-0.02	0.07	-0.04
Housing x. energy	20.2	0.1	0.4	-0.2	2.4	2.4	2.7	0.03	0.49	-0.04
Furnishing	6.9	2.1	0.2	1.9	7.6	9.5	6.5	0.14	0.65	0.13
Health	3.4	0.1	0.3	-0.1	3.4	3.2	3.4	0.00	0.11	-0.00
Transp. ex. gas, airl. tick	12.2	-0.0	0.3	-0.3	5.5	5.2	5.5	-0.00	0.63	-0.04
Airline tickets	0.8	3.7	0.2	3.5	20.3	19.3	10.0	0.03	0.15	0.03
Communication	2.4	3.3	0.0	3.3	1.8	5.2	1.8	0.08	0.12	0.08
Recreation, culture	10.8	1.6	0.1	1.5	5.5	7.1	5.4	0.18	0.77	0.17
Education	0.5	-	-	-	2.3	2.3	2.3		0.01	0.00
Restaurants, hotels	5.6	0.5	0.2	0.3	6.8	7.4	7.1	0.03	0.42	0.02
Other	8.7	0.4	0.3	0.1	2.7	3.0	2.8	0.03	0.26	0.01
CPI-ATE, s.a	93.7	**0.5**	**0.3**	0.2	**5.7**	**5.8**	**5.5**			0.21
Norges Bank est.			*0.5*		*5.7*		*5.7*			
Imported	36	0.8	0.2	0.6	6.0	6.4	5.5	0.28	2.33	0.22
Domestic	57	0.3	0.3	-0.0	5.7	5.8	5.5	0.17	3.31	-0.02
Energy, housing (x s.a)	4.4	-3.7	0.0	-3.7	12.7	0.8	5.1	-0.16	0.04	-0.16
Energy, transport (x s.a)	2.0	-8.8	-5.0	-3.8	26.8	15.8	20.6	-0.17	0.31	-0.07
CPI Total	100	**0.1**	**0.0**	0.1	**6.5**	**5.9**	**5.9**	0.08	5.89	0.06
Norges Bank est.			*0.2*		*6.5*		*6.0*			

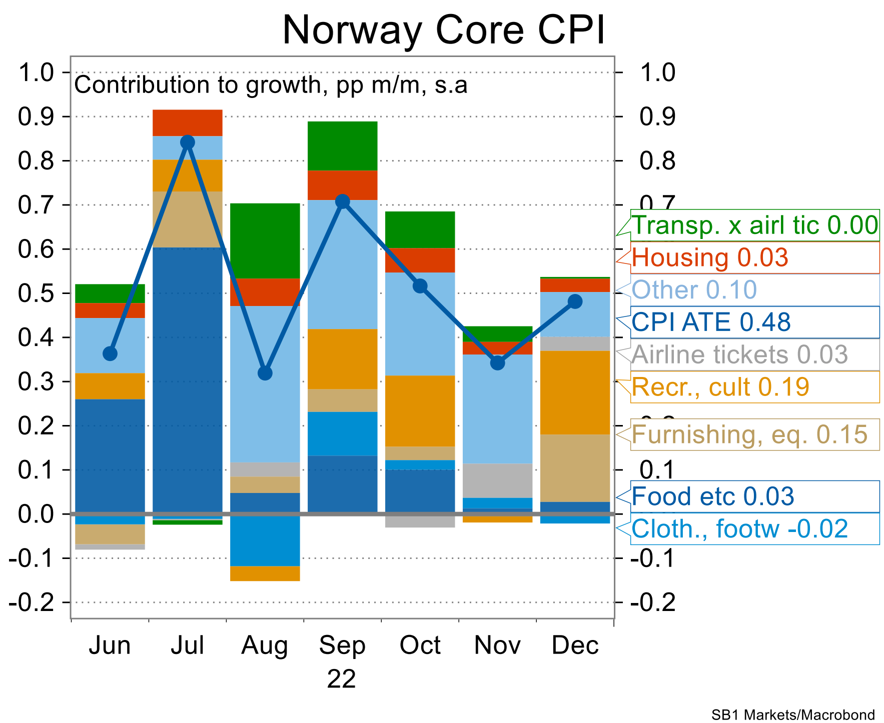
- **Food, non-alc bev.** prices rose 0.2% (ex taxes, seas. adj), we expected a 0.3% increase. The annual growth decreased 1.1 pp to 11.5%. The 'real' inflation is far lower
- **Clothing** prices fell 0.4% m/m, and are up just 1.4% y/y, 0.9 pp below our expectations
- **Furniture/hardware/equip.** prices were up 2.1% m/m and the annual rate rose by 1.9 pp to 9.5% - as household textile prices shot up!
- **Transport ex. gas & airfare tickets** was unch., and is up 5.2% y/y, surprisingly low given global auto prices
- **Airline tickets** prices were up by 3.7% m/m and are up 19% y/y, from a low level last year
- **Recreation** prices were up 1.6%, and are up 7.1 y/y, due to PC/TVs
- **Restaurant/hotel prices** up 0.5% m/m, 7.4% y/y

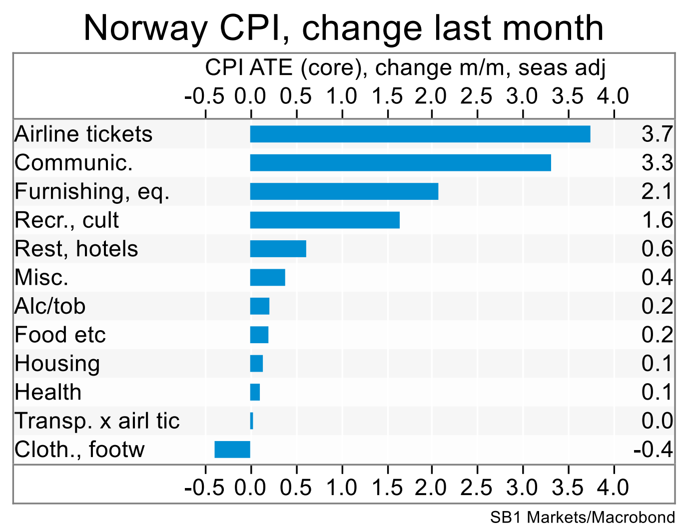
- **CPI-ATE** up 0.5% m/m, 5.8% y/y, 0.3 pp above our forecast, 0.1 above the consensus and NoBa's f'casts
- Prices on **imported goods** rose 0.8%, and are up 6.4% y/y – a substantial contribution to the total (2.3 pp), not due a NOK impact but due to high inflation abroad
- Prices on **domestically produced** goods & services were up 0.3%. The annual rate at 5.8% is remarkably high
- **Electricity (and other heating)** prices declined 3.7%, we expected unch.
- Gasoline/diesel prices fell 8.8% m/m, we expected -5.0%
- … **headline inflation** fell to 5.9%, in line with our expectations but 0.2 pp below consensus, 0.1 pp below NoBa's estimate

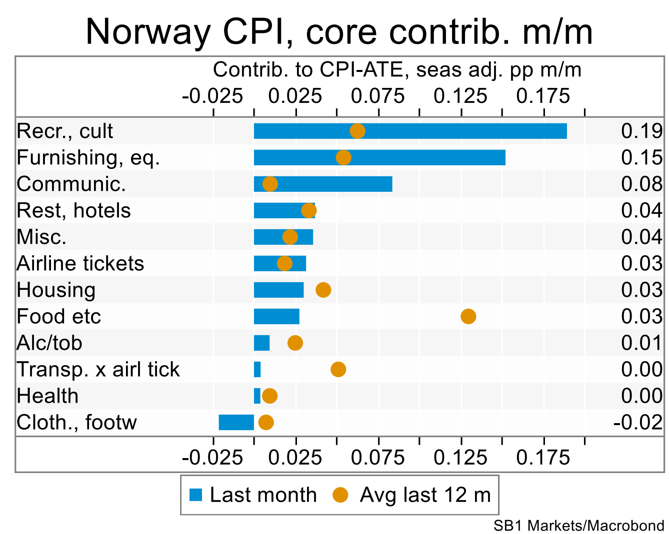
Monthly changes are seasonally adjusted by SB1 Markets. The weighted sum of the components does not necessarily sum exactly up to the total, and deviations m/m and y/y do not necessarily add up. Norges Bank m/m s.a. estimate is implied, calculated by us. Sources: SSB, Norges Bank, SB1 Markets calculations

Data eq/TVs, cell phones & subs., househ. textiles the December story!

Food price inflation has slowed the past two months

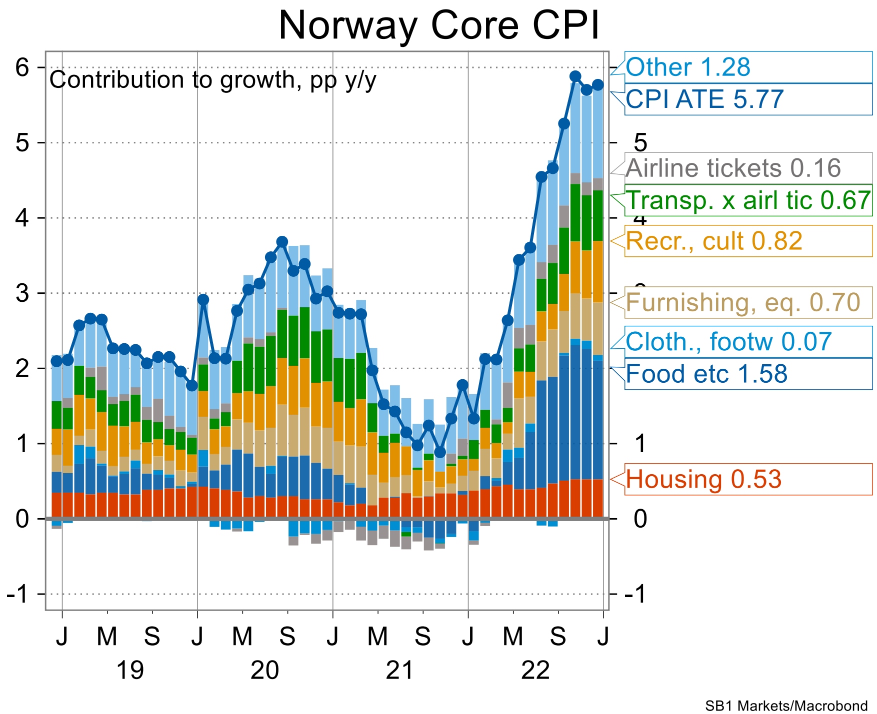


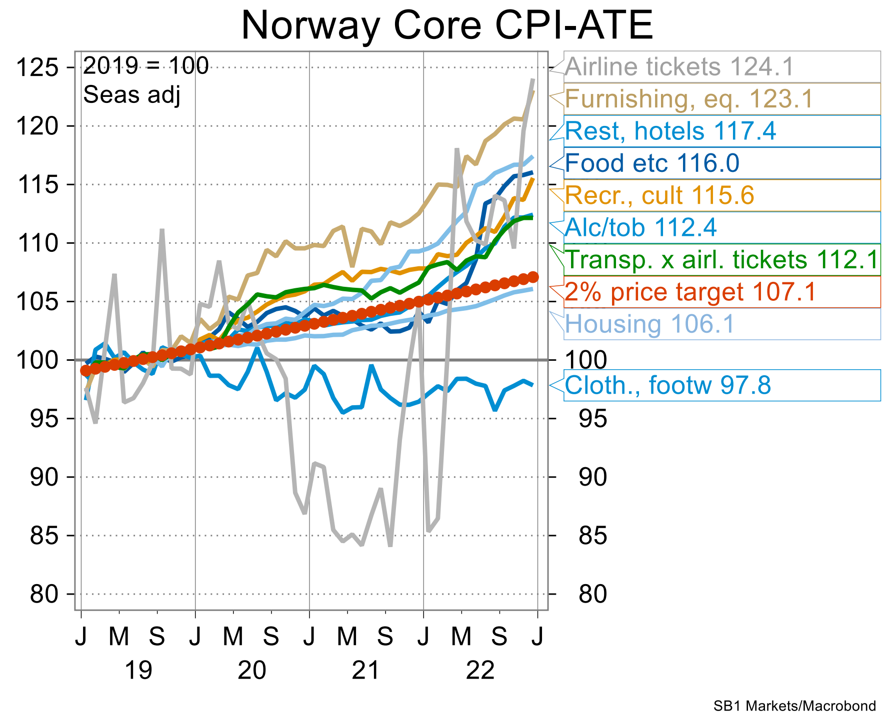




The core rate may have peaked, but it remains too high – broad based

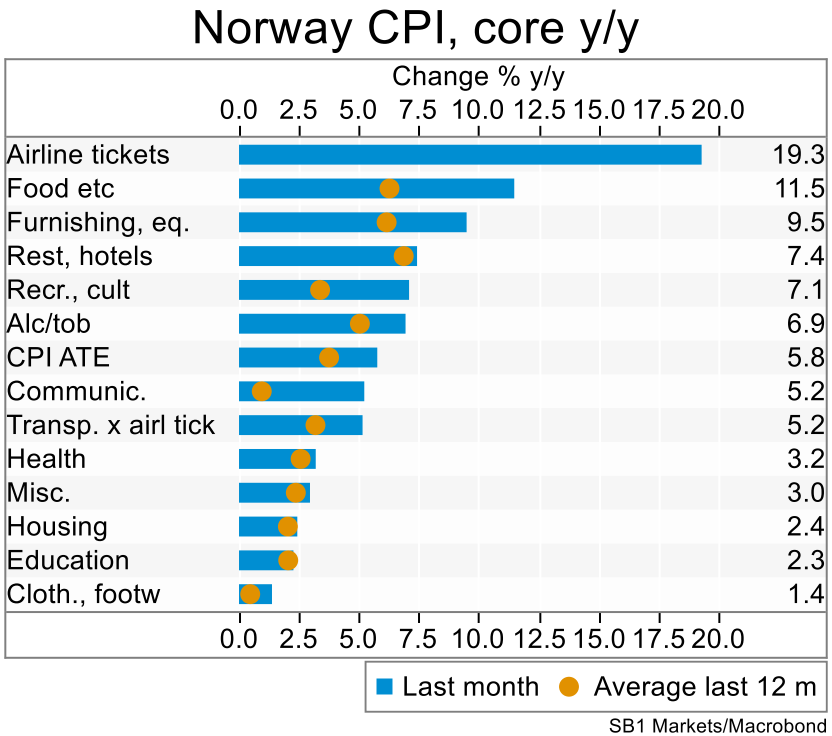
Just clothing/footwear, and housing ex energy below the 2% path since 2019

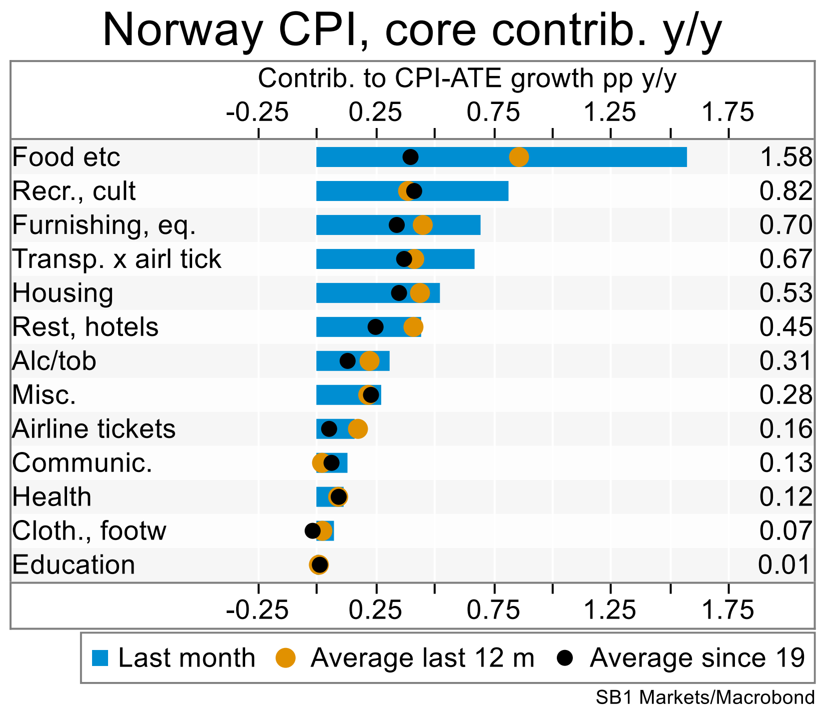




12 sectors report core inflation above 2.0%, just 1 is below

Food, transportation, recreation, housing, and furnishing have contributed the most y/y

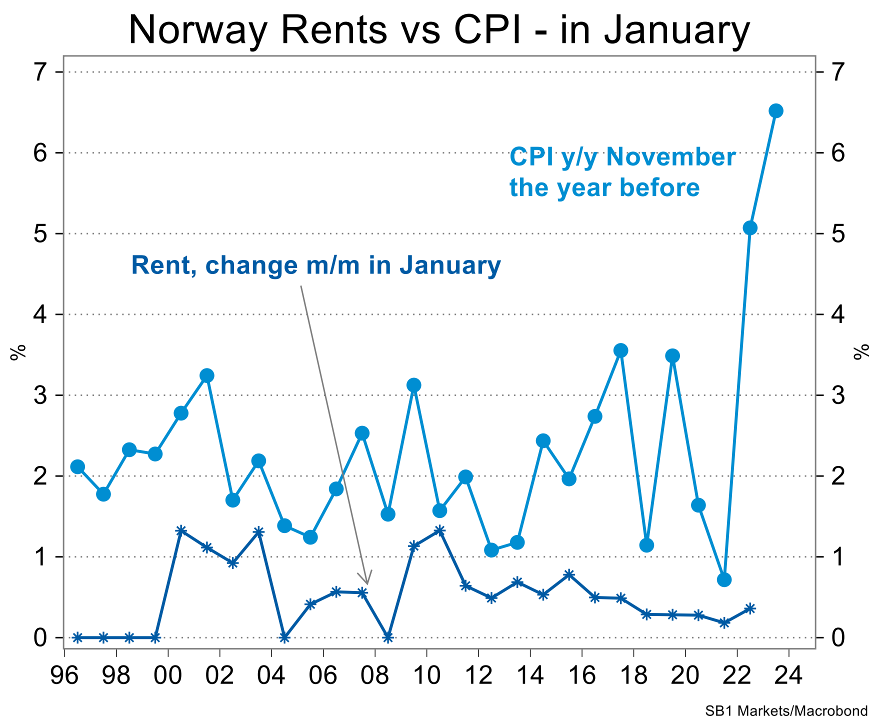


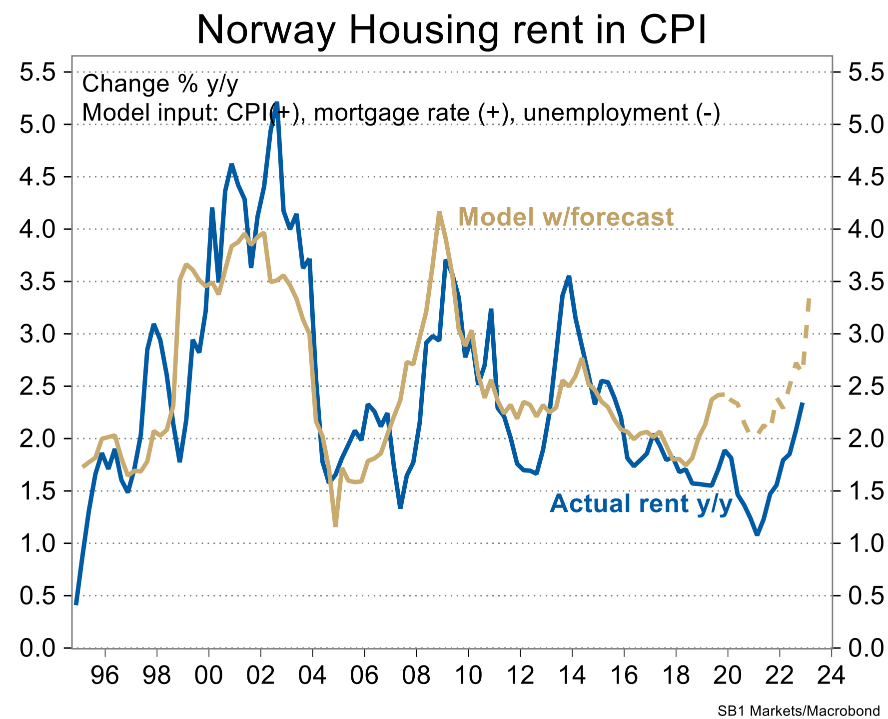


- 81% of sub-components of the CPI are up more than 2%
- **52% are up more than 5%**

Rents, the next shoe top ‘drop’ (or rather ‘take off’?)

No reason to expect a shock in Januar – but the outlook is not that good…



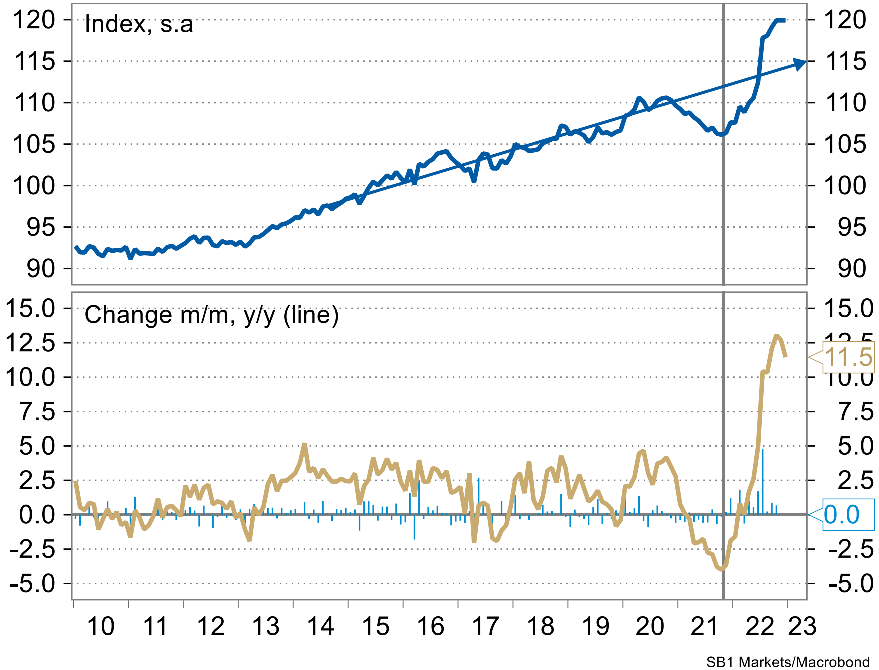


- **There is no correlation** between changes in rents in January, vs the CPI growth in November the year before (the last CPI print available before rents are set in January)
- However, changes in CPI inflation have an **clear impact** on rents, with a 3 – 6 quarters lag. In addition, the mortgage rate has a positive, while the cycle, here the unemployment has a negative impact
- Given the surge in CPI inflation the recent quarters, it is likely that rent inflation as it is measured in the CPI will accelerate form the present 2.4% y/y growth rate – feeding back to the CPI etc. An increase to 4% rate of rent inflation from the present 2.4% will lift the CPI by some 0.3 pp vs.
- In the Norwegian CPI, the rent component is an average of actual, observed rents, and a calculated owner’s equivalent rate. The two are very closely correlated

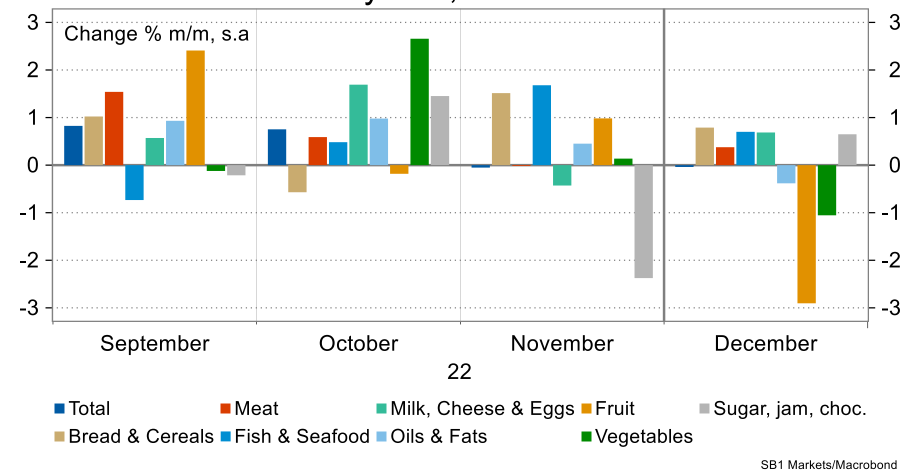
Food prices are up 11.5% y/y, but ‘just’ 5% above trend-path

If prices had not fallen sharply through

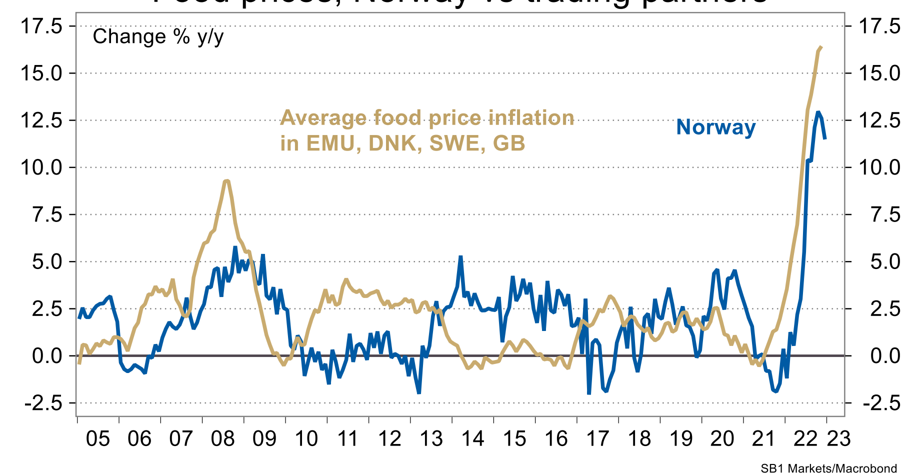
Norway CPI, Food & non-alc beverages



Norway CPI, Food details



Food prices, Norway vs trading partners

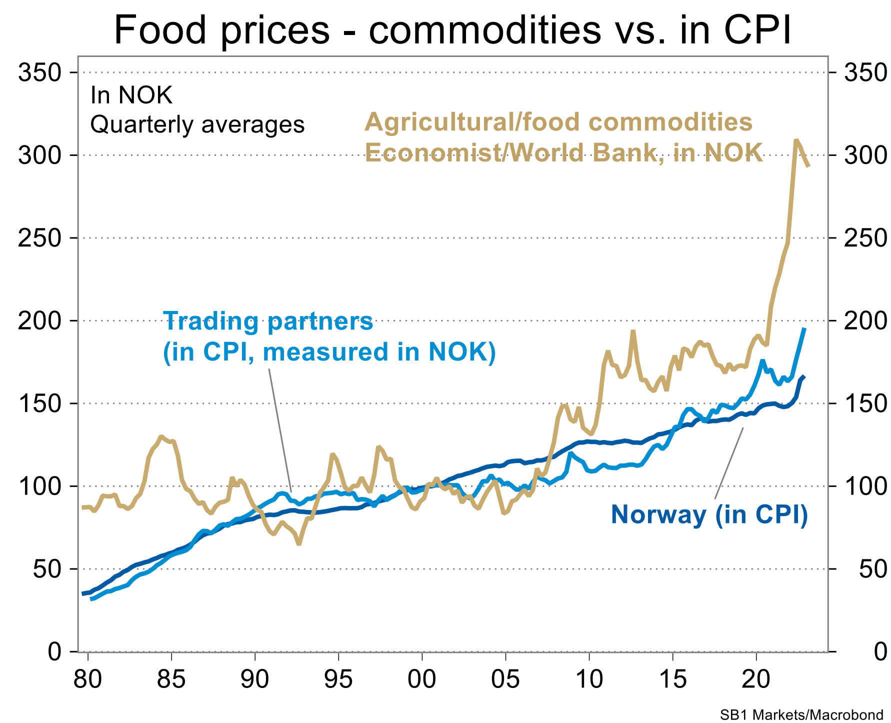


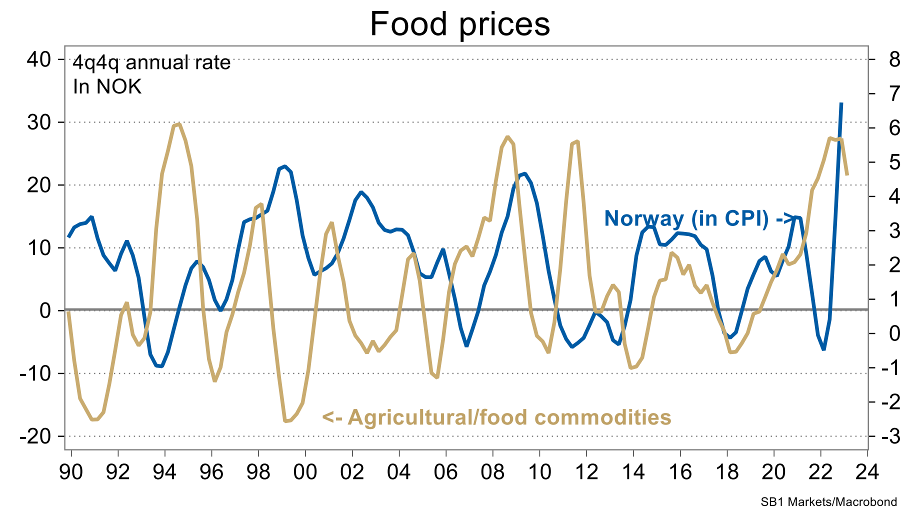
- Prices were close to flat m/m, and up 11.5% y/y (slightly down from the peak at 13.1%). Fruit prices fell m/m (-3%), as did vegetables and oils – all other articles were up in price
- Norwegian food price inflation is lower than among our neighbours, not an encouraging sign – even if the correlation has been non-existing
- <u>The good news now: Food prices (commodities) are trending down globally (at least measured in until recently USD)</u>

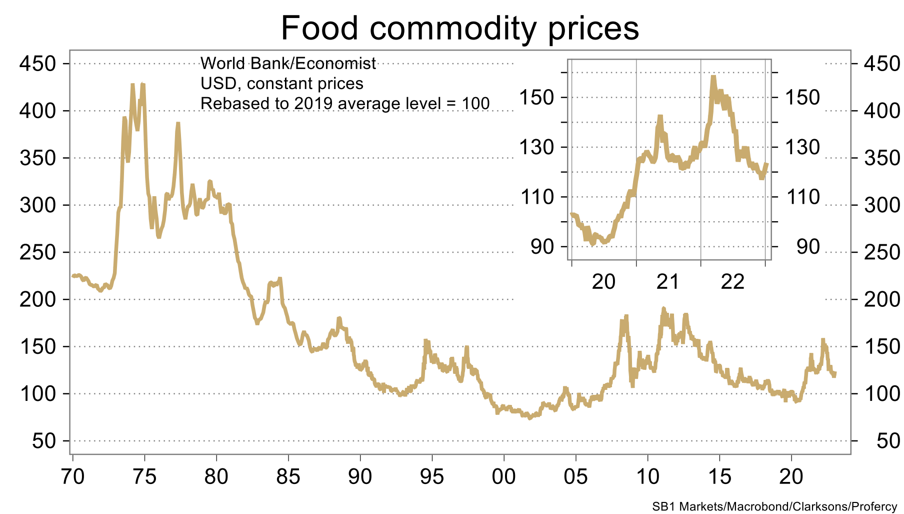
SpareBank 1 MARKETS

Food commodity prices: Limited correlation to trading partners' food prices

… And no stable correlation to Norwegian food prices (in the CPI). Now, food commodity prices have peaked



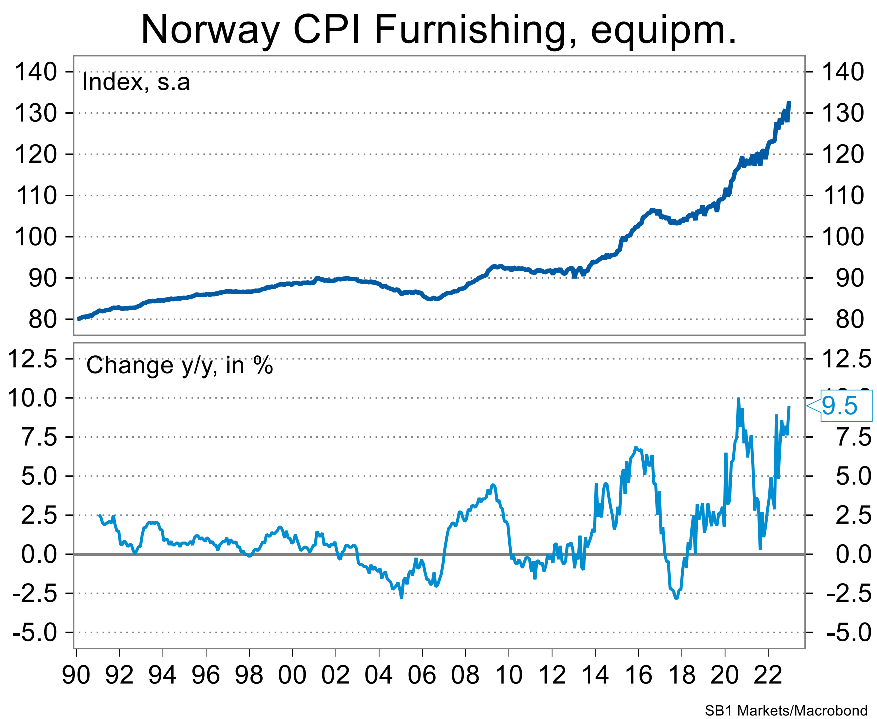


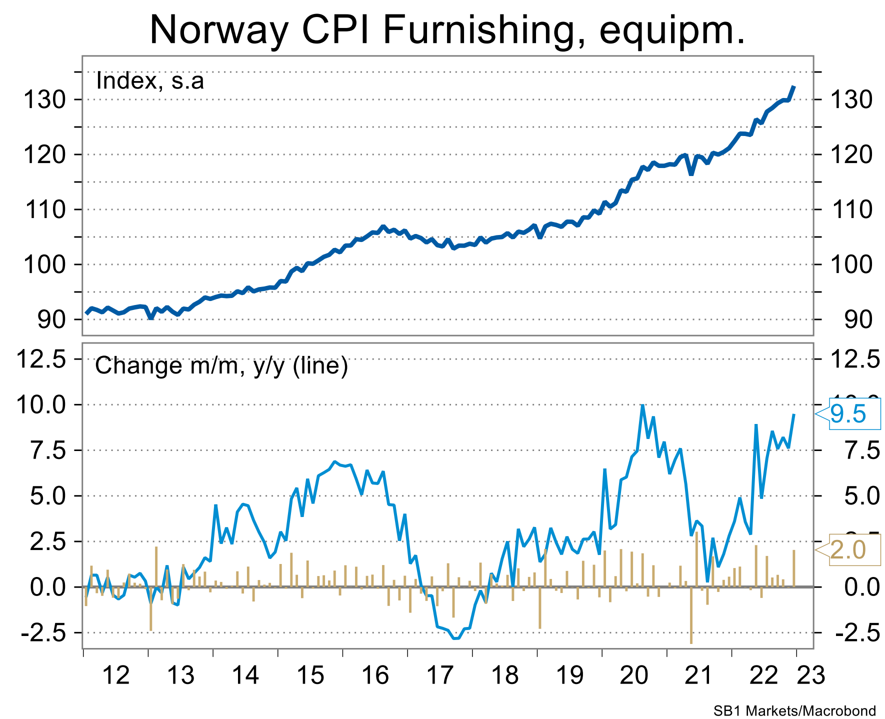


- Agricultural/food commodity prices are sharply up from mid 2020 but have fallen sharply since March in USD terms. In real USD terms, prices are below the past 10 y average. However, measured in NOK, prices are not that low…

Furnishing etc. suddenly up 2% in December – and prices are up 9.5% y/y

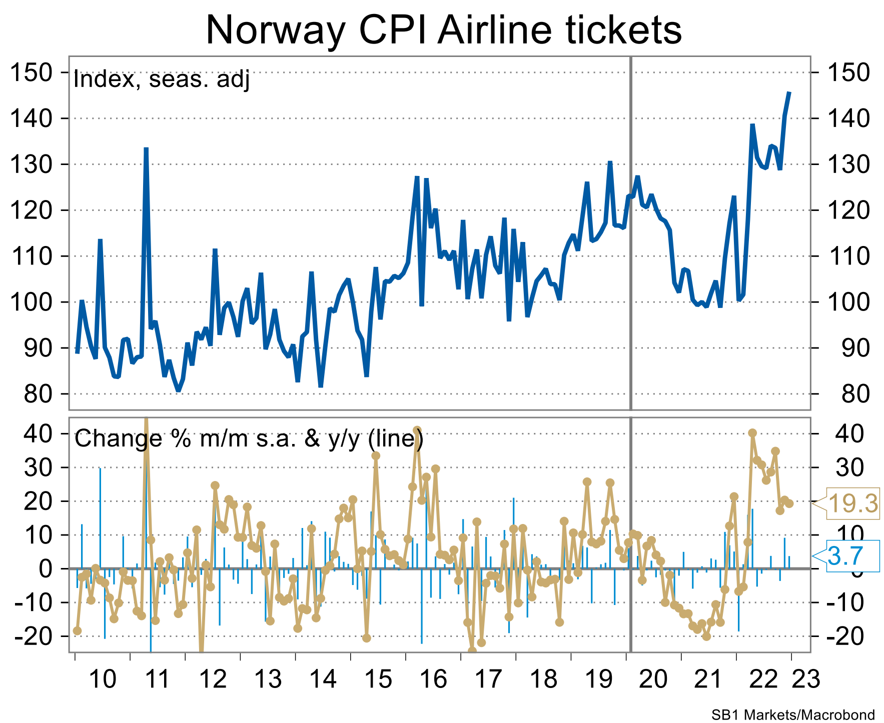
The main contributor in December: Household textiles (up almost 15% m/m!)



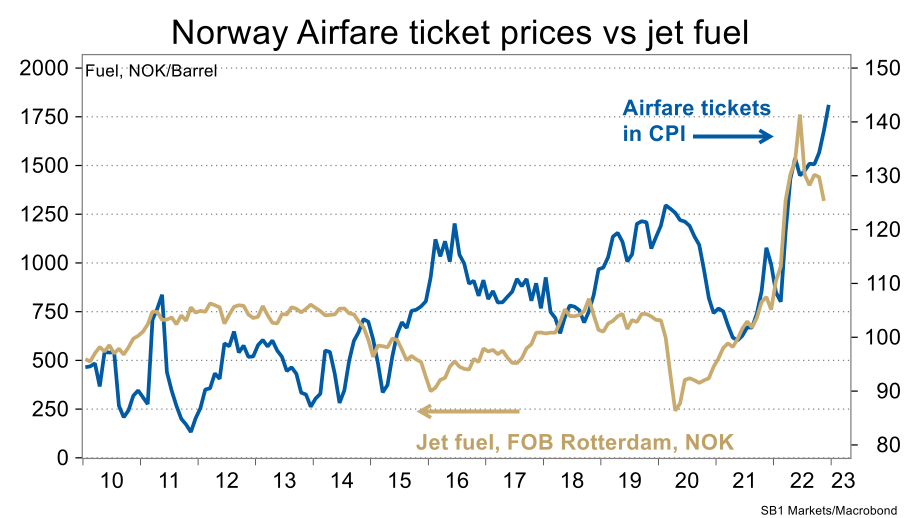


Airfare ticket prices further up in December

Prices are clearly above a long term trend (2¼ % per year) - and should be, given the fuel cost

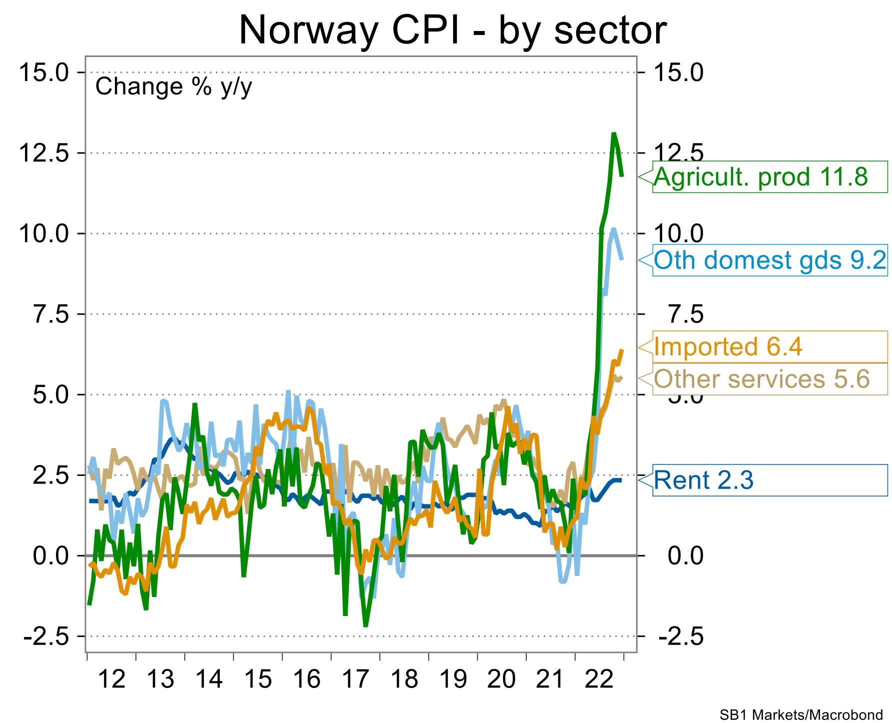


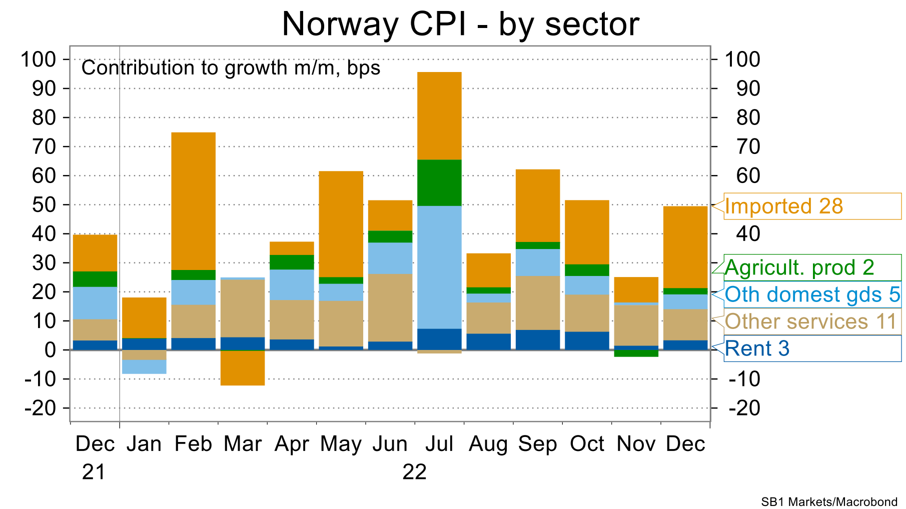
- **Airfare ticket prices** were up 3.7 m/m in. Prices are up 19.3% y/y, contributing 0.16 pp to the annual core rate
- **Prices** are some 10% above the pre-corona trend path – which could at least partly be explained by the increase in the fuel cost
- However, there is no historical correlation between ticket prices and the **fuel cost**, check the chart below (and fuel prices have fallen 18% since June)

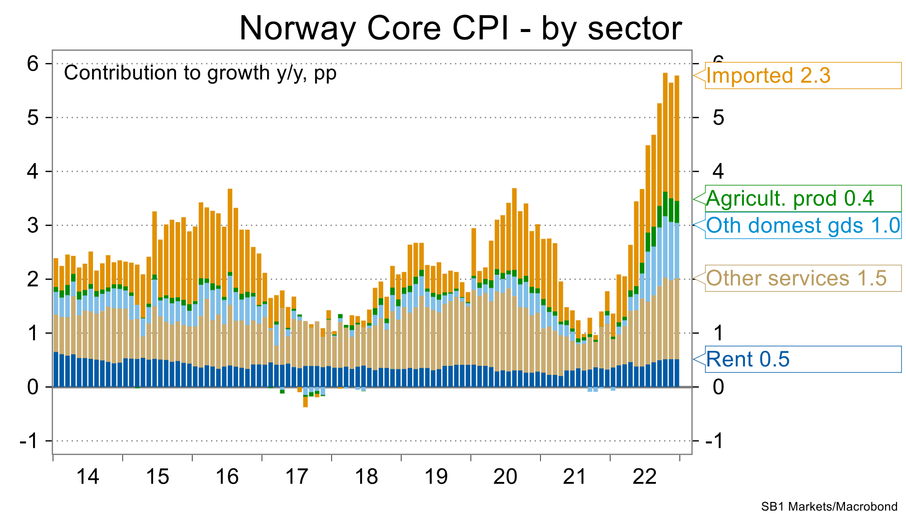


Imported goods contributed the most in December

… but domestic goods & services the most over the past 12 m. Domestic goods up 9.7% y/y, services (x rents) 5.6%



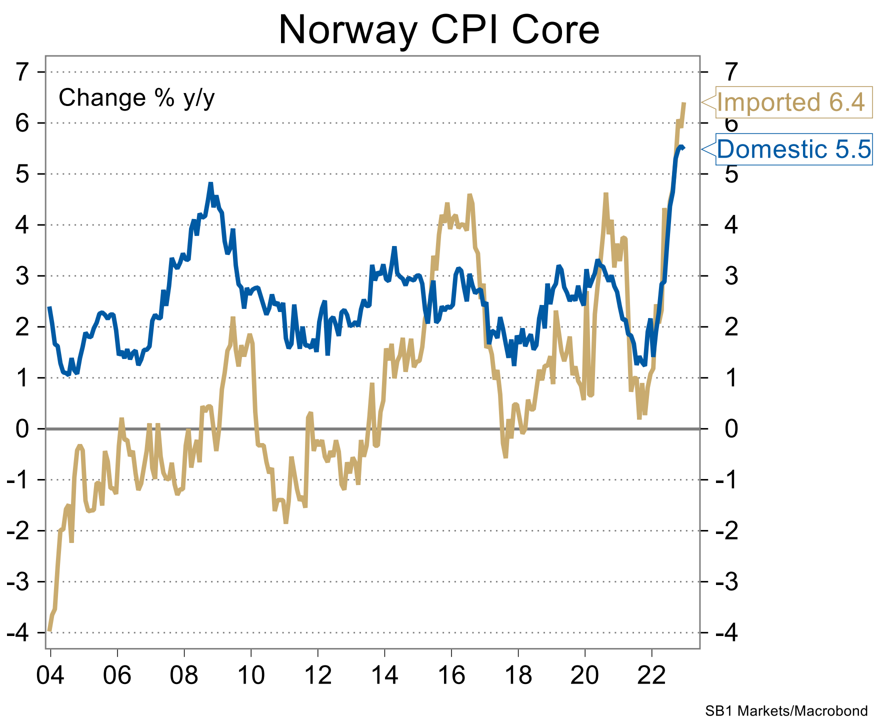


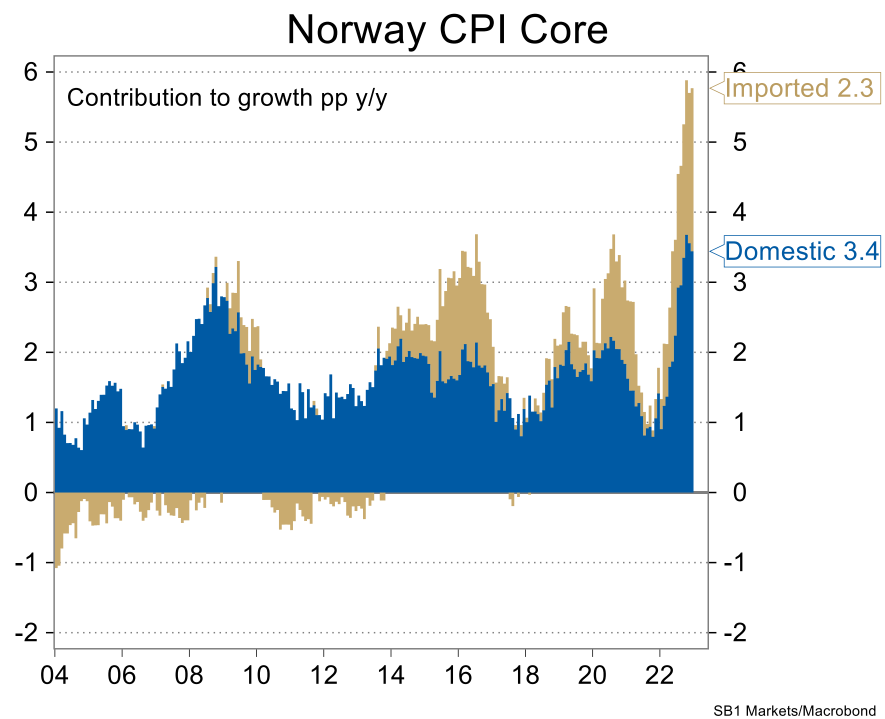


- **Domestic services inflation ex rents** slowed sharply during the corona crisis, and is now climbing faster, up 5.6% y/y, contributing 1.5% to core inflation, with hotels/restaurant and recreation/culture (partly services) contributes the most
- **Domestically produced agricultural products** are up 11.8% y/y, contributing 0.4 pp to the overall core rate
- **Other goods** than agricultural & imported products, that is goods produced in Norway are up 9.2% y/y, and contributed 1.0 pp to the core inflation rate
- **Rent** inflation is still modest, at 2.3%, yielding a 0.5 pp contribution

Both imported goods and domestically produced goods & services contribute

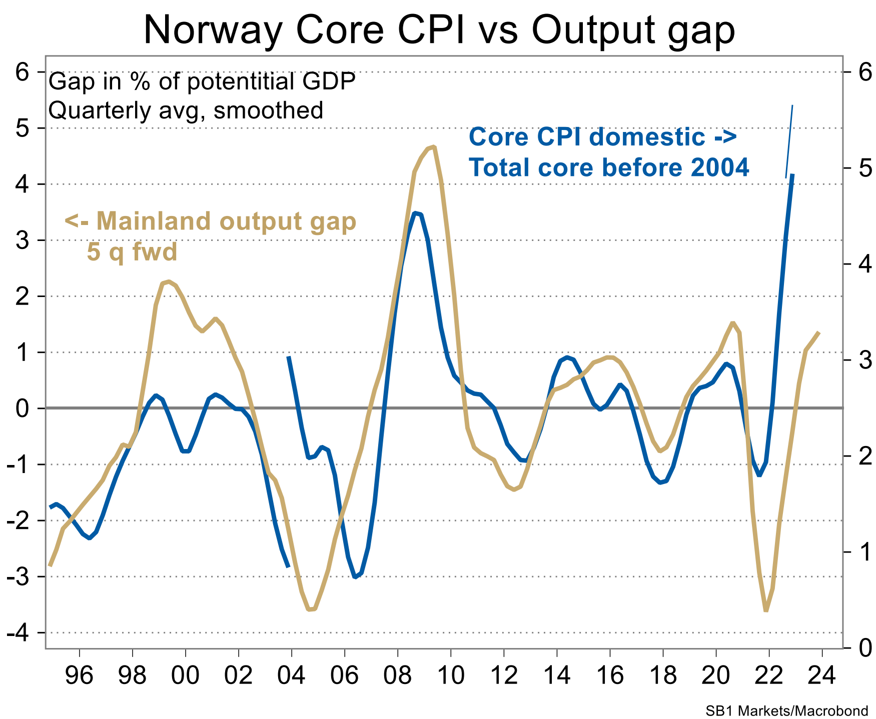
… and the domestic component is by far the largest contributor

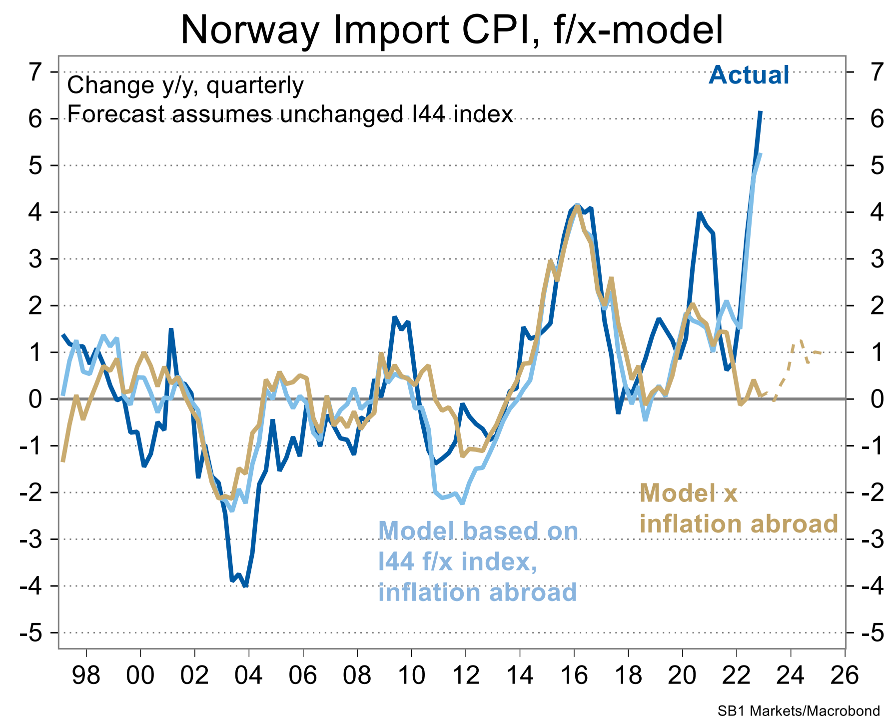




Domestic inflation up due to a strong domestic economy? At least partly

... but the lift has arrived earlier than normal, and it is larger. ‘Imported’ inflation close to the model estimate

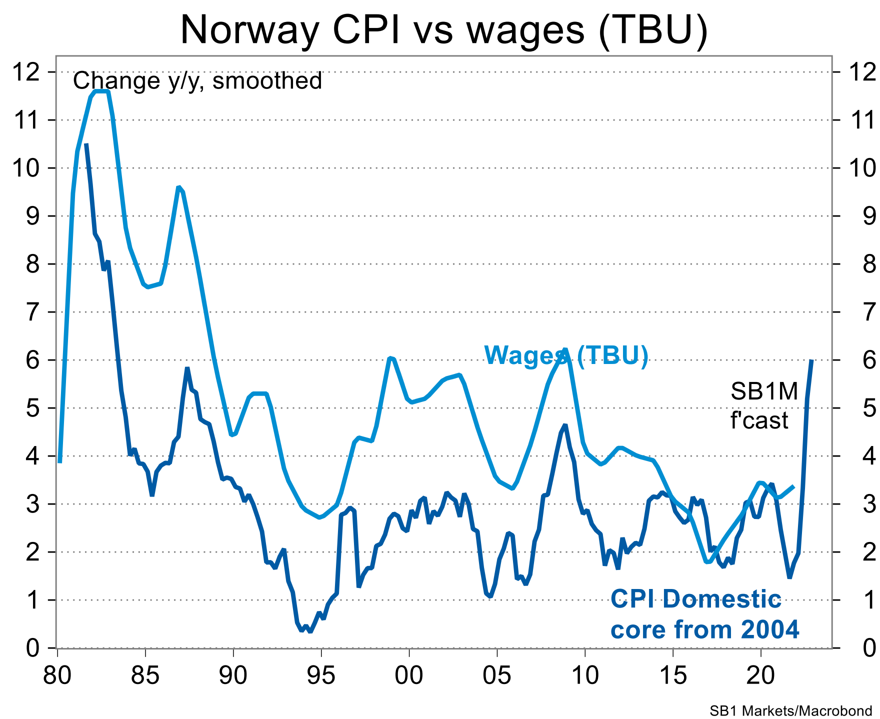


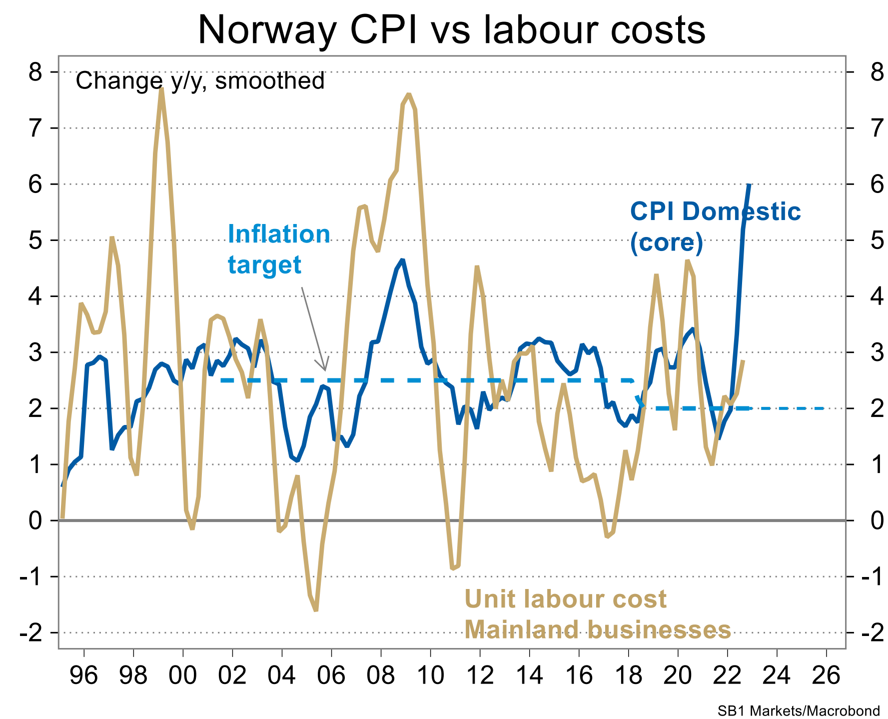


- **… if inflation abroad** is included in the model, together with the exchange rate. If inflation abroad is **not included**, imported inflation is underestimated by close to 6 pp. Thus, the ‘weak’ NOK is not to blame for higher prices on imported goods, but rather high inflation abroad
- **Labour market data and surveys as well as Norges Banks’s estimate,** indicate that the output gap is higher than the mechanic calculation on the chart to the left (that is more of the domestic inflation is ‘explained’

Domestic costs: Weak productivity growth is lifting unit labour costs

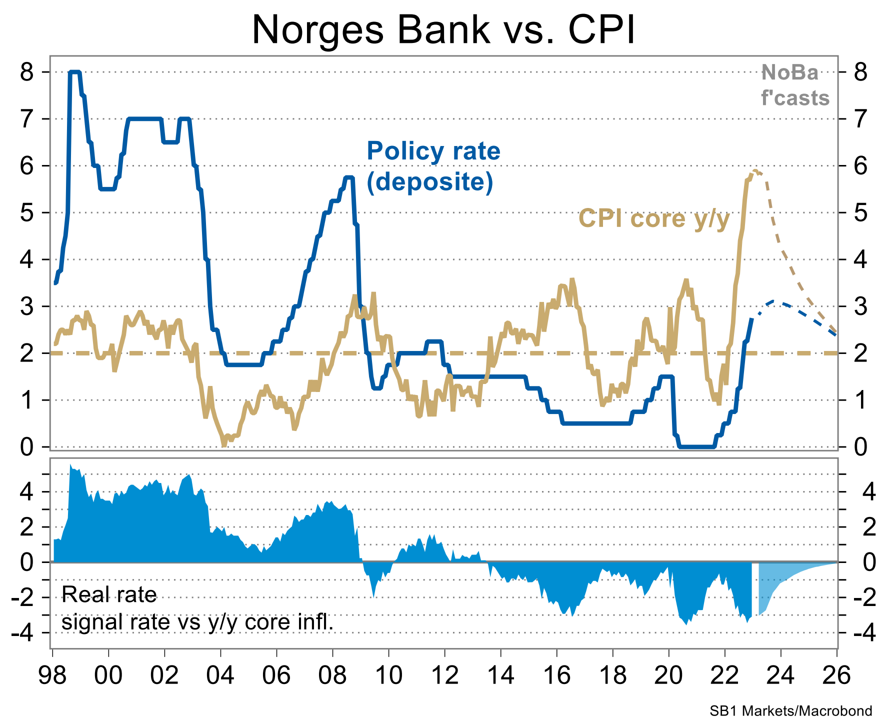
But wage inflation has not accelerated (we thought it would), and ULC is up less than 3% y/y (but that's still rather high)

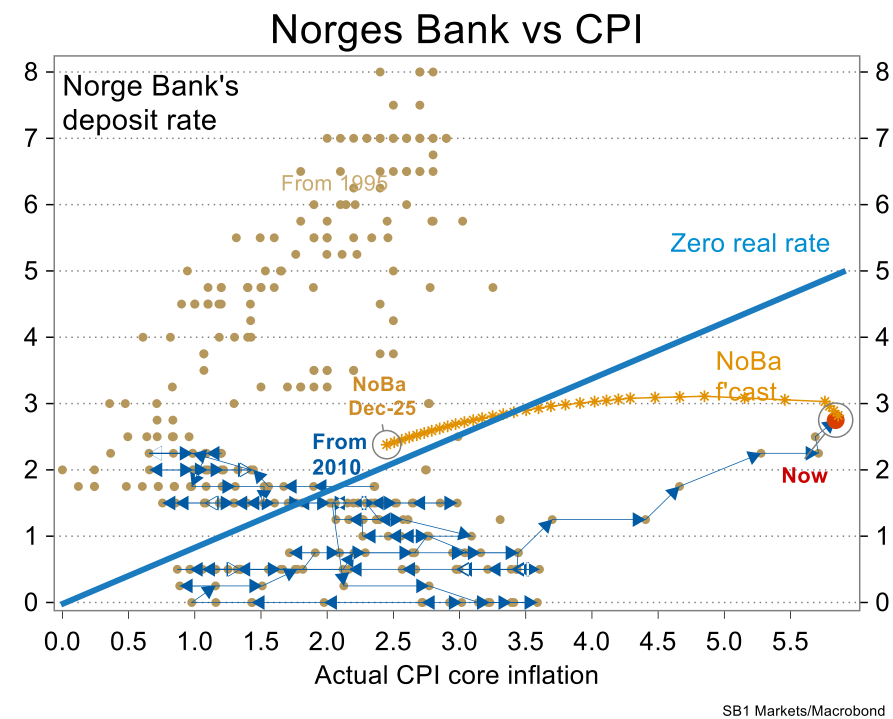




- Unit Labour Cost is us some 3% y/y

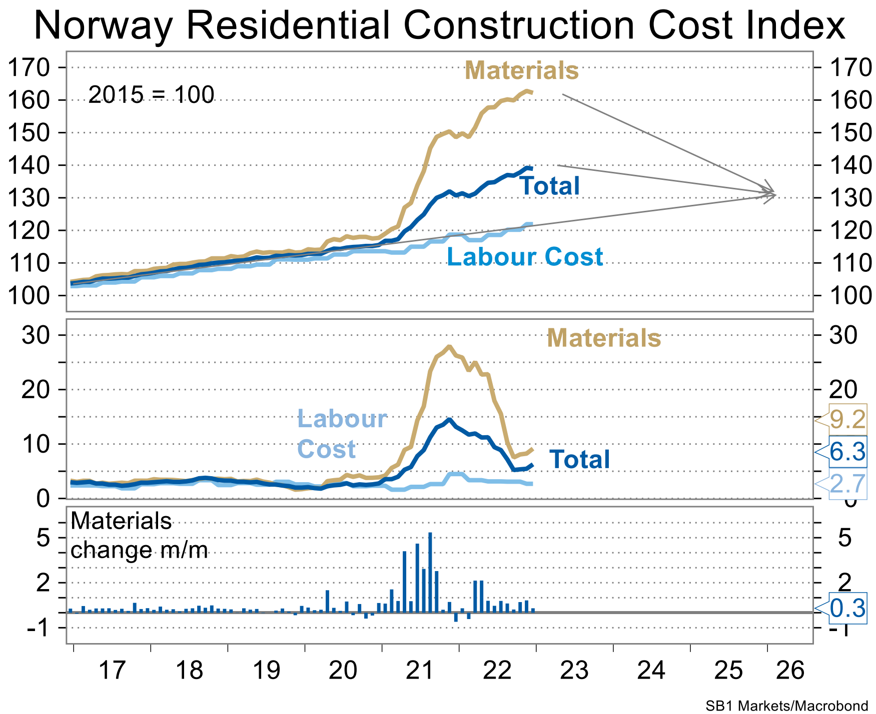
The lift in the core rate is not good news – but it was in line with NoBa expect.

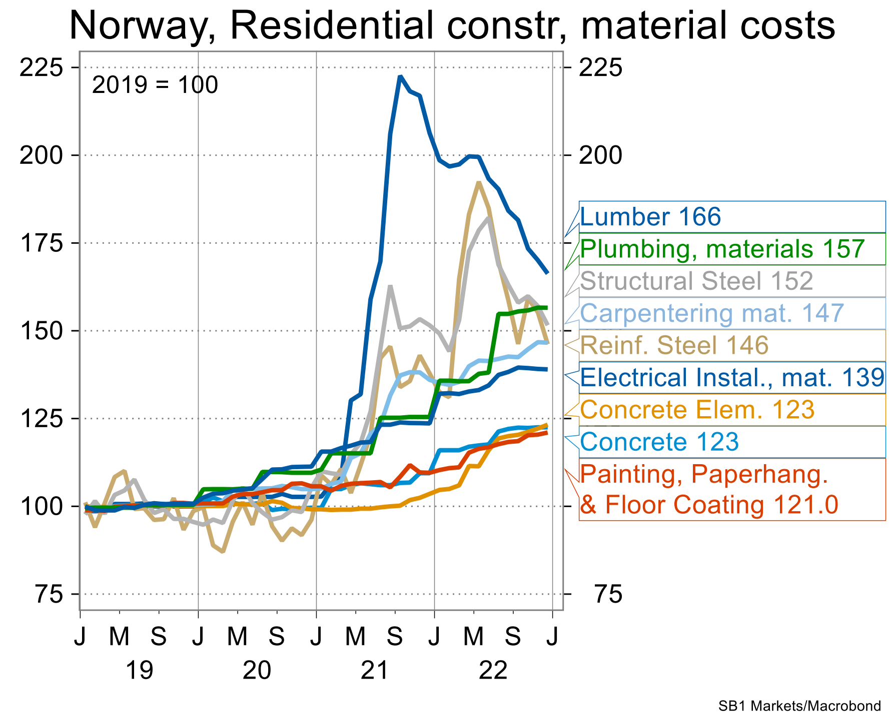




Building material prices still on the way up, even if lumber & steel are falling

We are quite confident, material prices will soon decline. No signs of any labour cost inflation

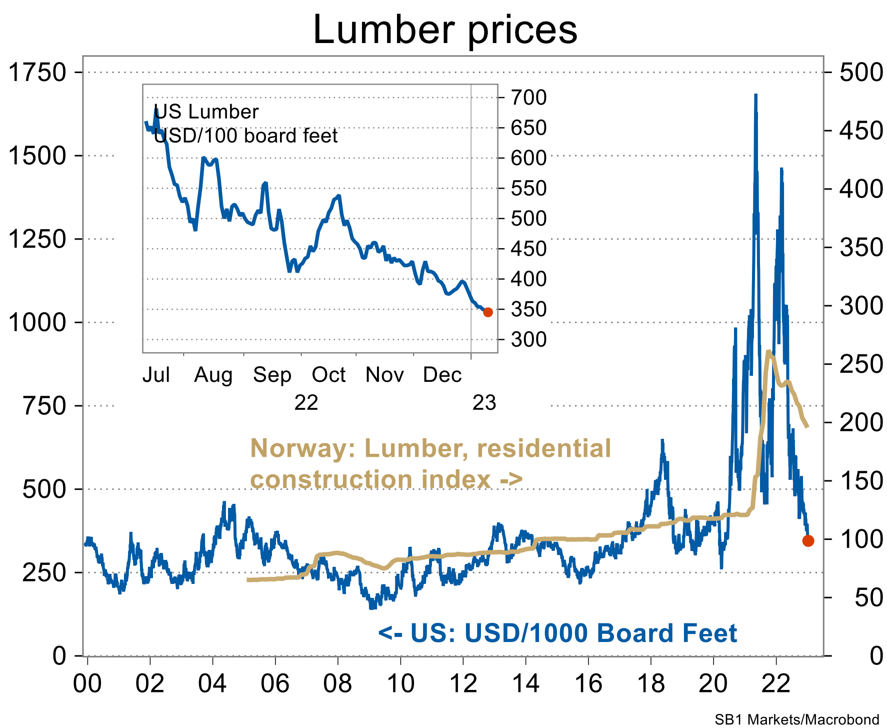




- **Material prices** (houses and apartments) added 0.3% December. Prices are up 9.2%, down from 28% at the peak
  - Lumber prices are trending down, and reports signal further declines the coming months. Steel prices also fell in December but these prices have flattened recent months (in line with global steel prices)
  - Other material prices are still trending up; but slower. Plumbing materials, electrical equipment and concreate rose just sightly
- **Labour costs** were just up 2.7% y/y in Q4, down from 3.1% in Q3 – no sign of acceleration
- Including labour costs, the **total building** cost index is up by 6.3%, down from the ATH at 14.6% at the peak last Oct. The price level is up 13% vs. the pre-pandemic 2.5% growth path. <u>Going forward, we still think lower material costs will bring total construction costs down to more normal levels.</u> Upside risk: A brisk recovery in the construction sector in China, pushing steel and other globally traded construction related commodities upwards

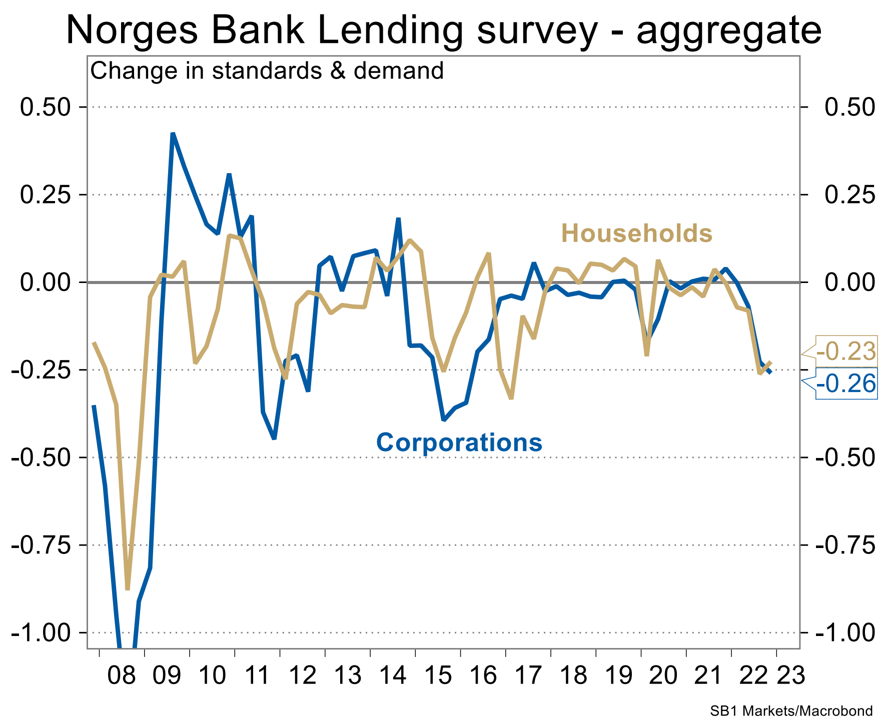
US lumber prices (2”x4) almost back to a normal level

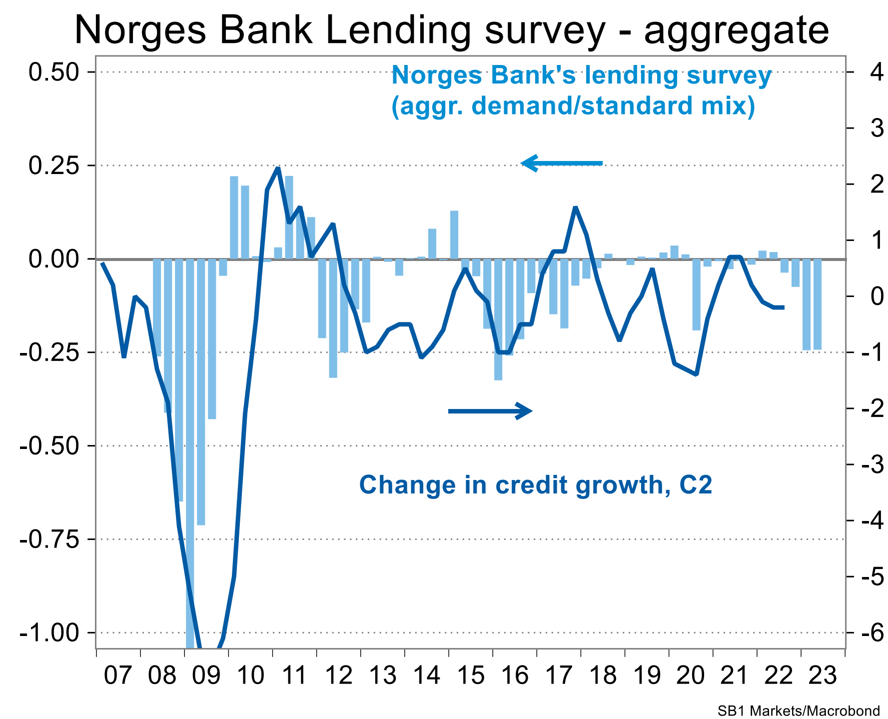
Steel prices are down from the peak, but bottomed during the summer. Now up on hopes of a Chinese recovery?



The credit cycle has turned – from the demand and the supply side

Demand is waning, both from households and businesses – but standards are not tightened by much



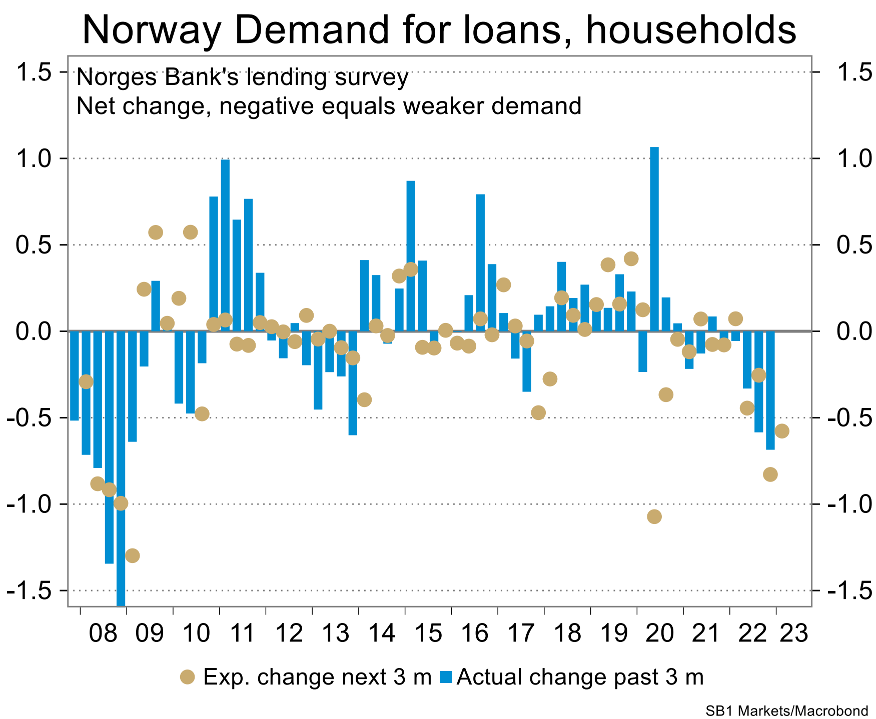


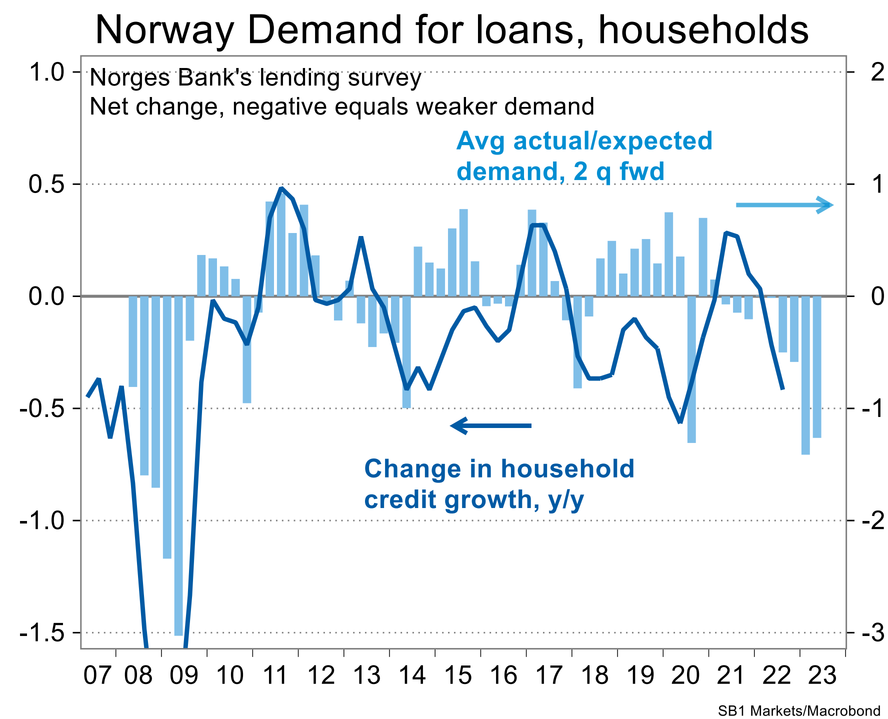
- .. And the there is sill no drama, neither vs. demand nor credit standards

Data in this section are seasonally adjusted

Demand from households weaker in Q4, as was expected…

…and the negative trend is expected to continue into Q1

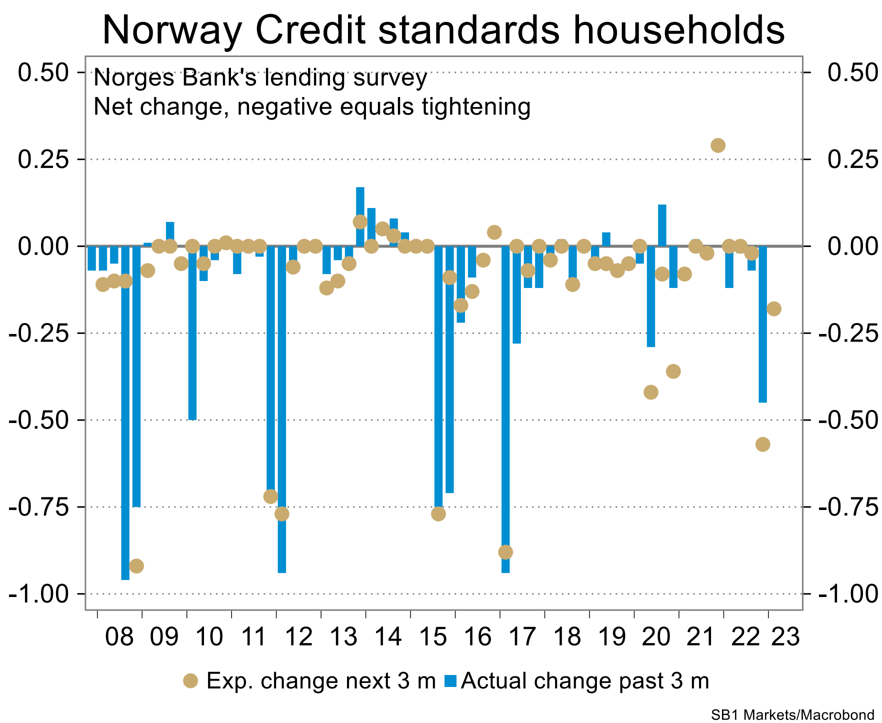


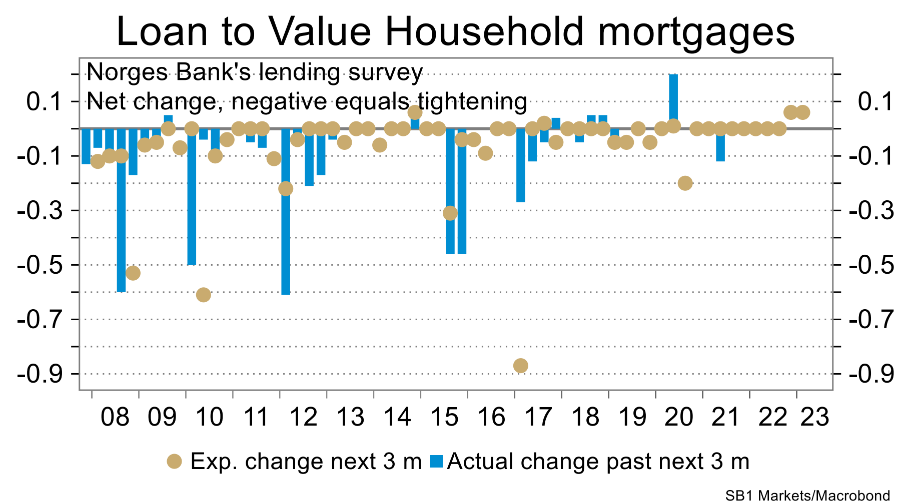


- There is not any tight correlation between banks' expectations for household demand for credit or their assessment of actual growth and the realised growth in household credit, as measured by the C2 credit indicator
  - Still, the lending survey probably tells the sentiment among bankers pretty well
  - The reported decline in demand the past two quarters as well as the expected decline in Q2 is not as harsh during the worst of the financial crisis (2008), but barring that period – when growth in household debt fell to 7% from 13% - the 2nd toughest change in bankers' assessment

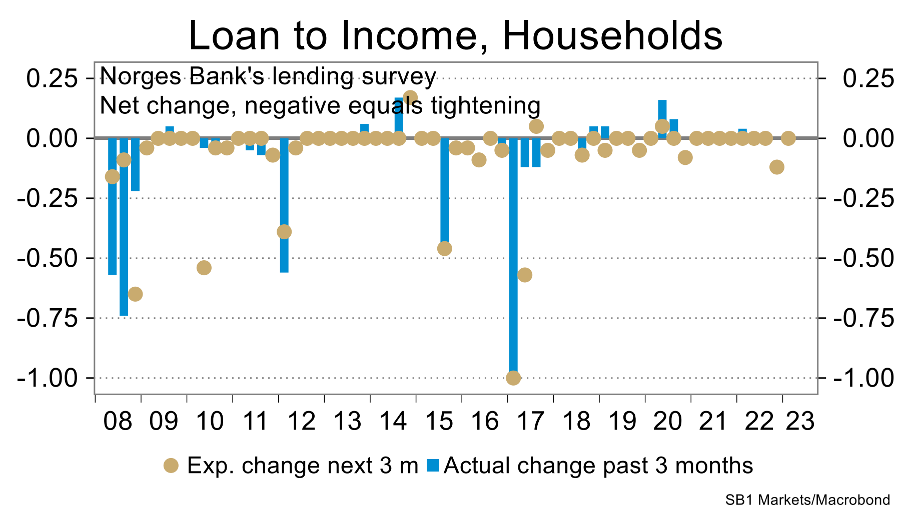
Some tightening vs households but we have seen more of it before

And it 'just' tighter instalment requirements, no changes so far in LTV of LTI standards



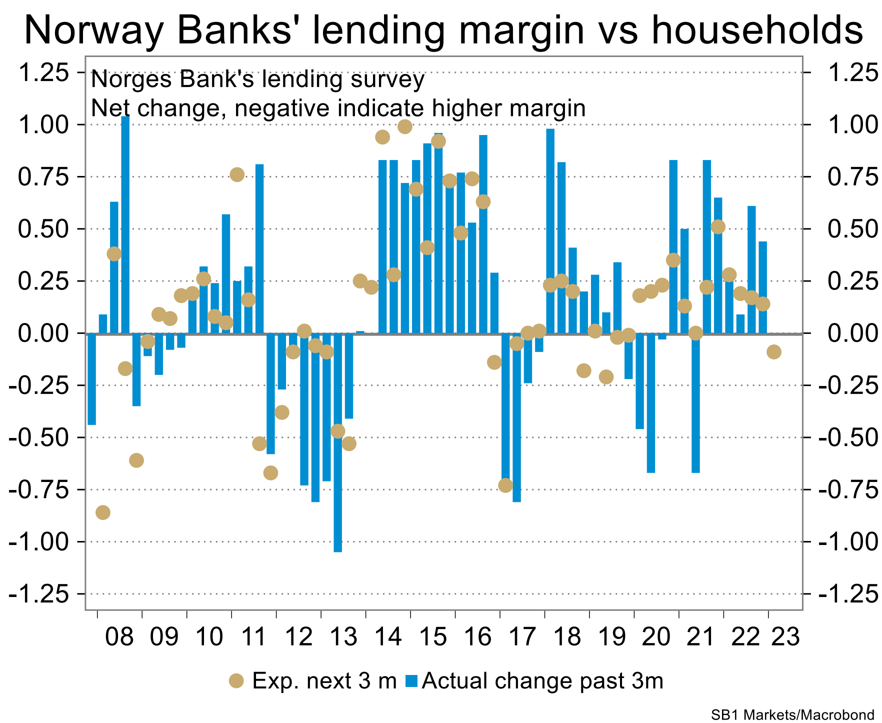


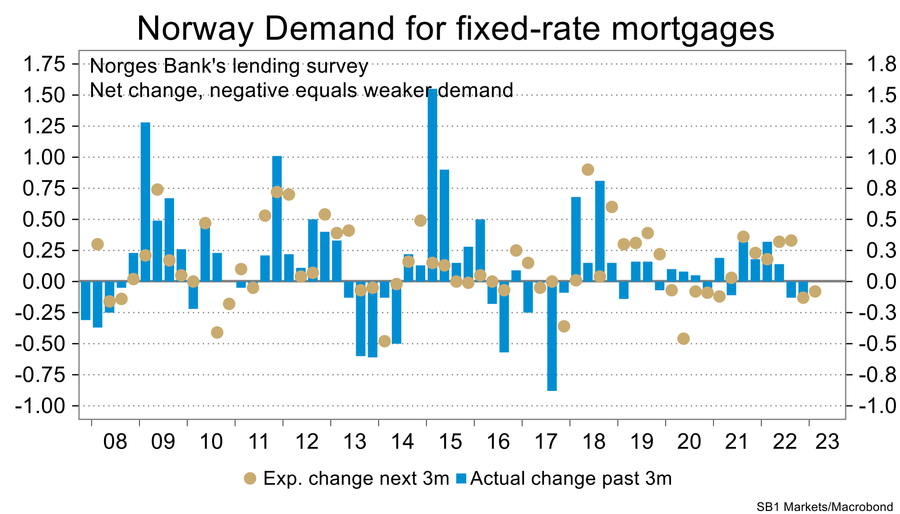
- Banks report that the **macroeconomic outlook** was the main reason for tightening standards (and not risk willingness, funding, capital requirements, delinquencies or losses)
- The only tightening element in Q4 (as in Q3 and expected in Q1) was **requirements for installments** (less are offered no installments than before)

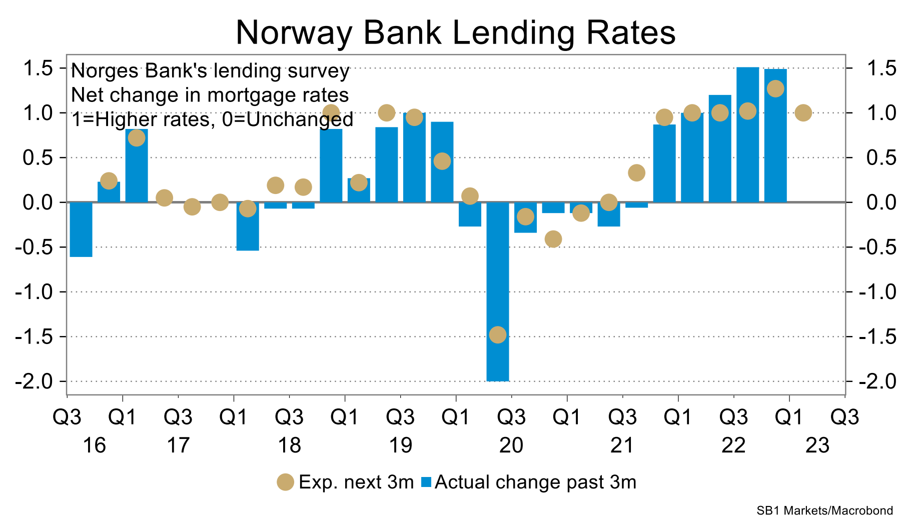


Banks decreased their lending margins vs households in Q4 but are hiking

Actual margins vs NIBOR have fallen, while spreads vs. deposits have increased, and in sum up



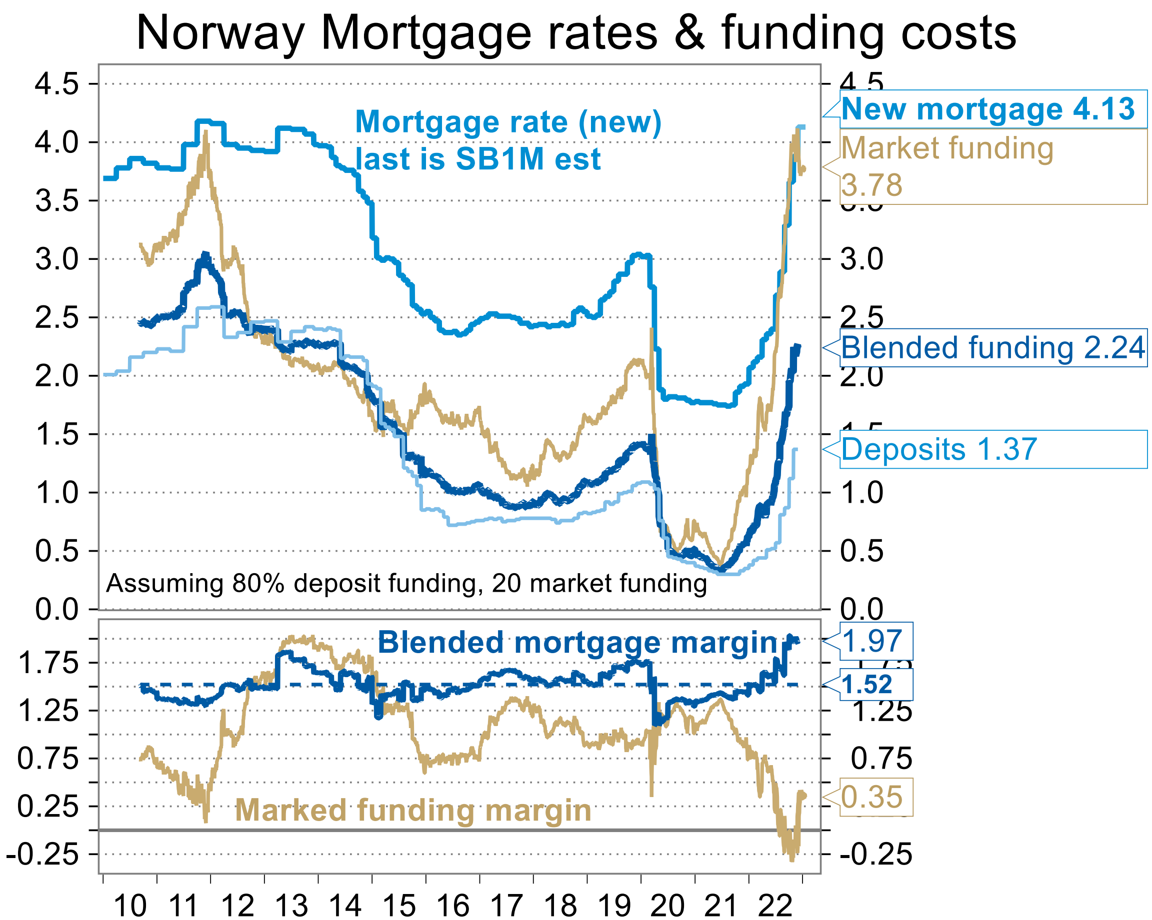




- Lending rates are of course on the way up – and are expected further up
- Demand for fixed rate loans fell in Q4-22 and is expected decline further in Q1-23. The fixed rate has become too high for comfort – or are households just smarter than the 'street' - and assume that the term premium is too high?

The best mortgage lending margin, ever?

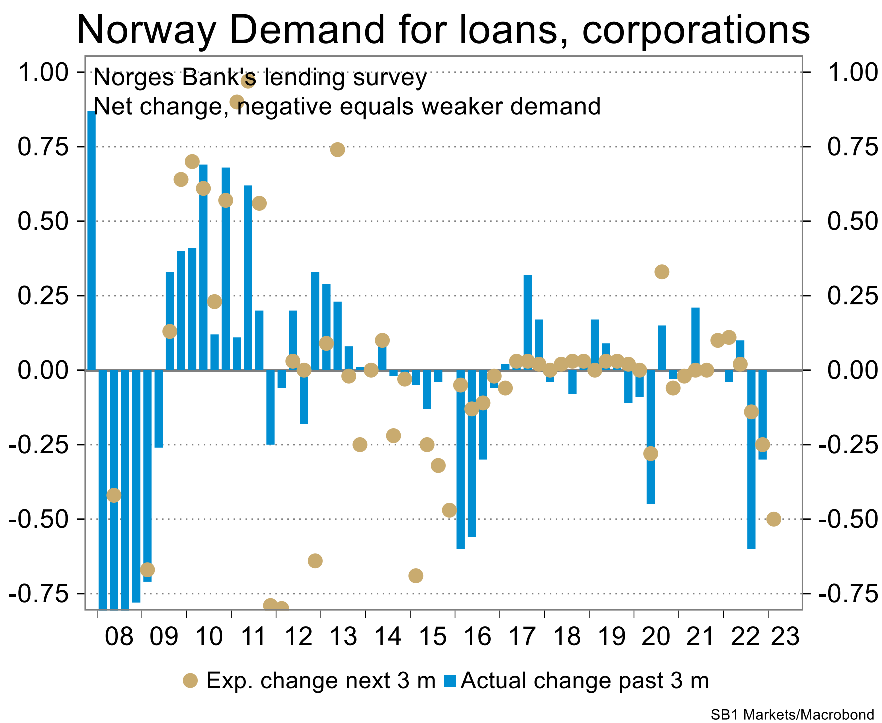
However, we assume deposit rate will continue to drift upwards even the NIBOR rate should stabilise at the current level

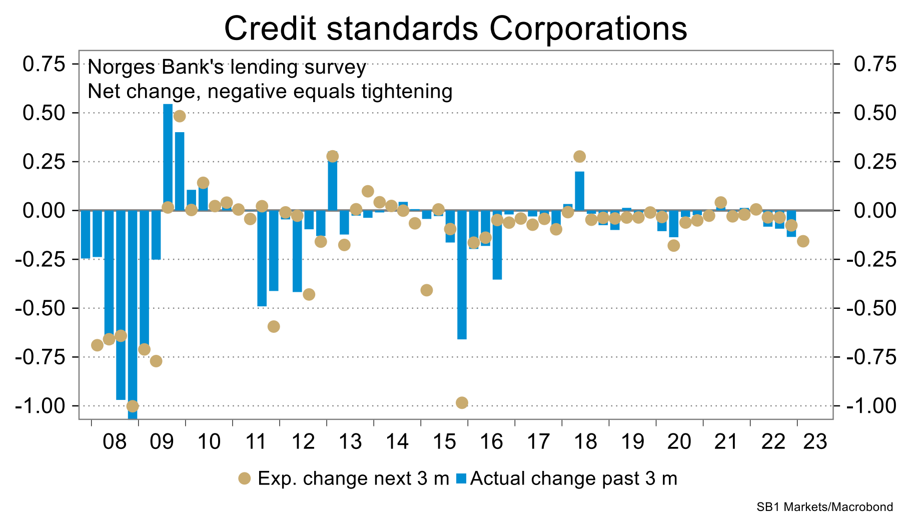


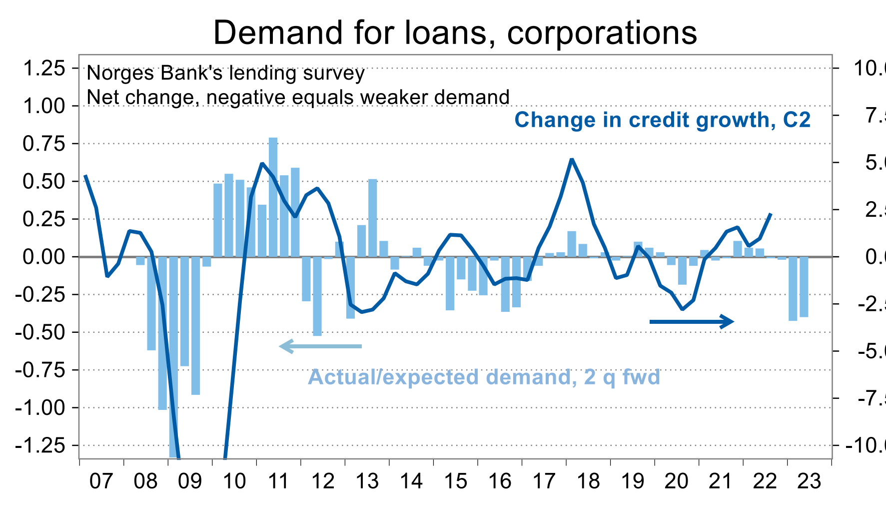
SB1 Markets/Macrobond

Demand for loans from businesses continued to fall in Q4

Demand fell far more than expected in Q4, and is expected to fall further in Q1



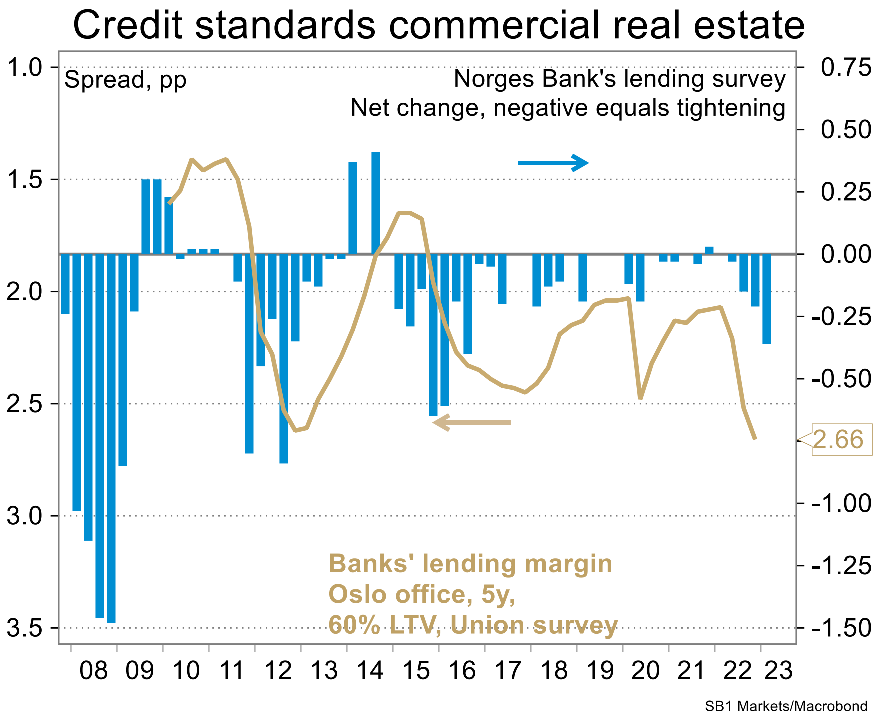


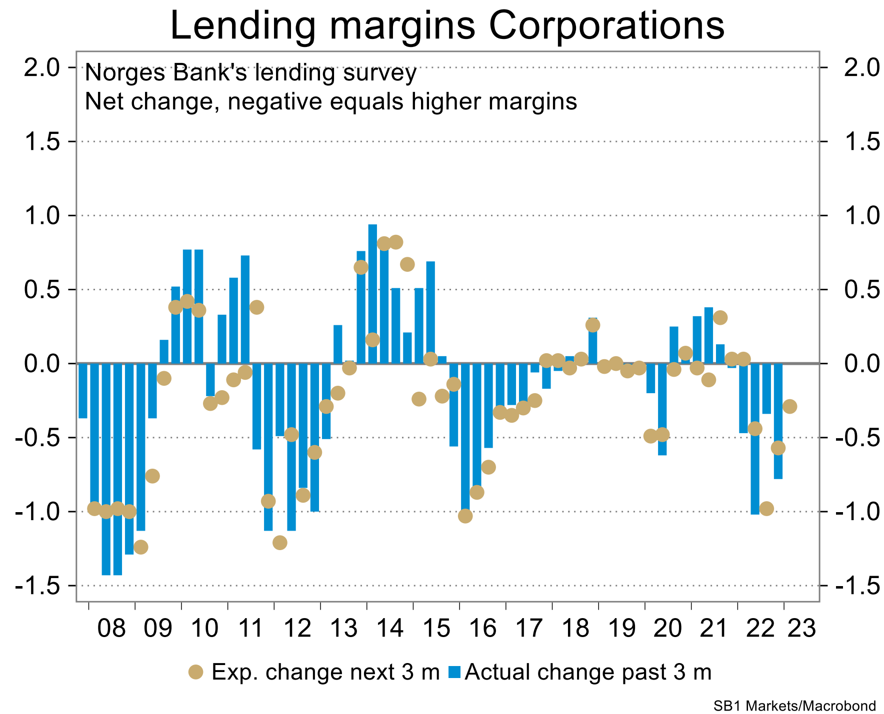


- Actual **credit growth** has accelerated recent quarters but given this survey, a slowdown is likely
- However, **credit standards** have been tightened somewhat, but not significantly

Tighter standards, higher margins vs. real estate + higher margins vs. all corps.

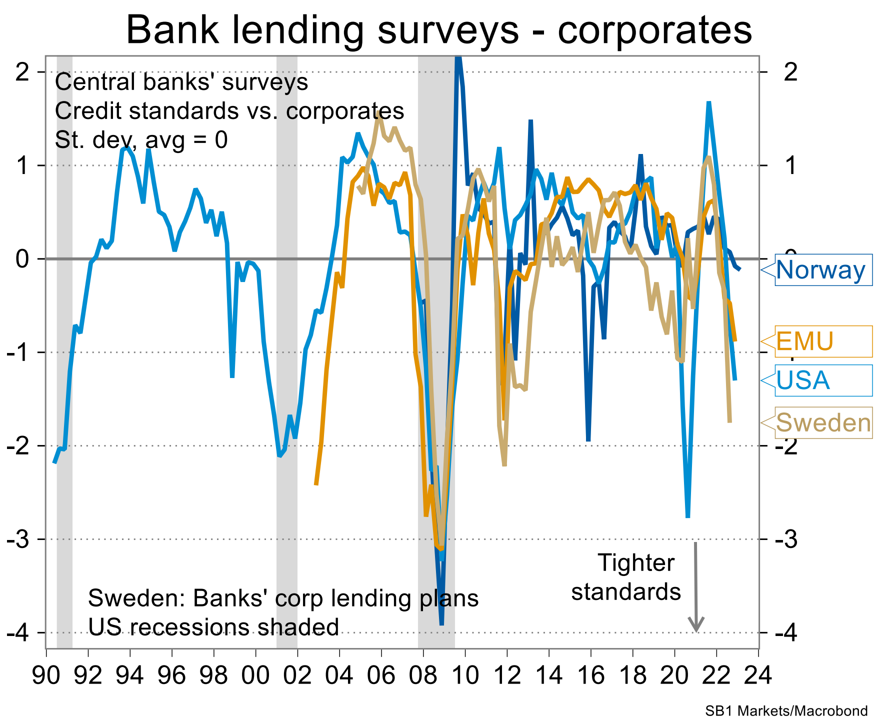
Banks increased their lending margin vs. businesses in Q4. More to come in Q1

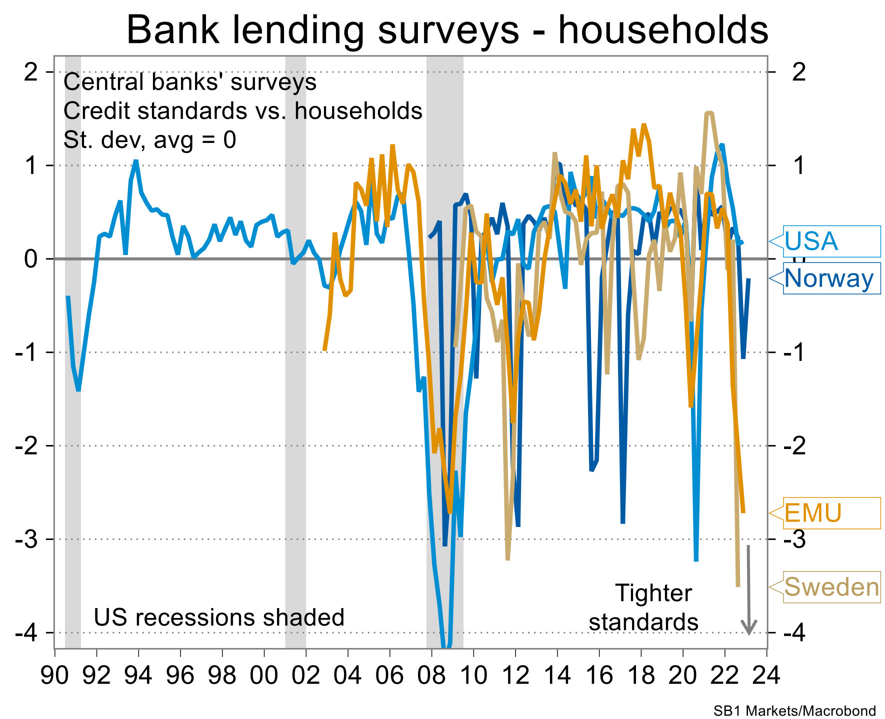




Global view: A substantial tightening everywhere – barring Norway??

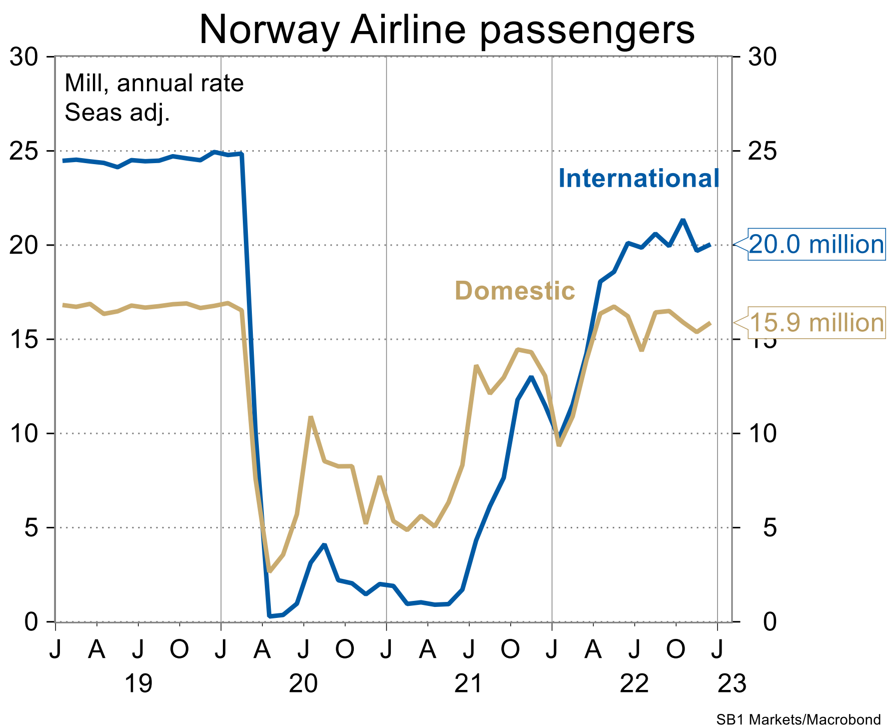
Norwegian banks an outlier? Seems so. Some tightening but nothing when compared with ROW. Rather surprising

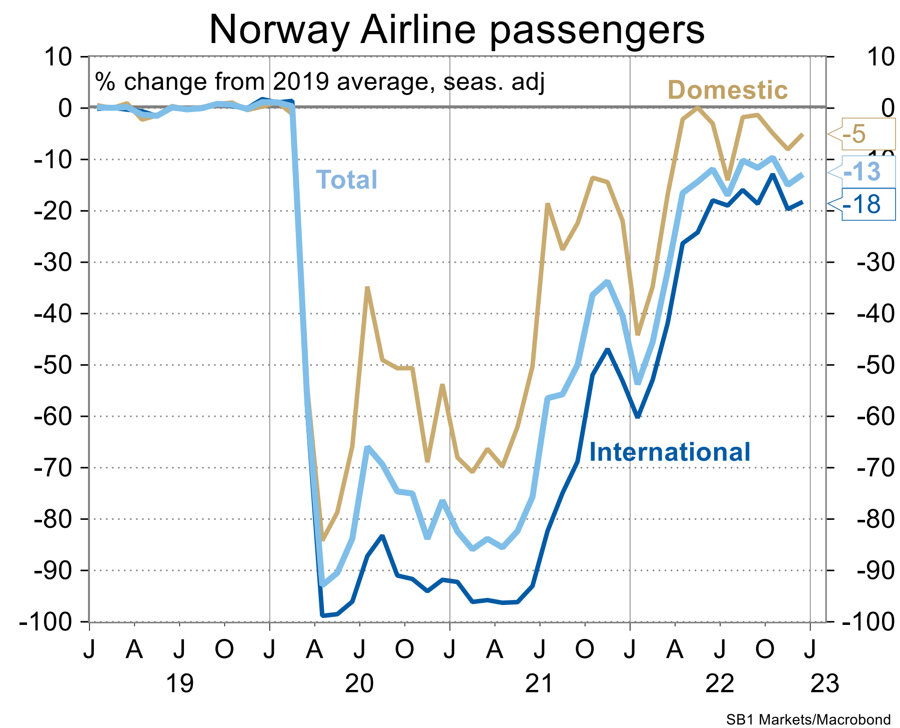




Airline traffic has flattened; Domestic down 5% vs 2019, internat. -18%

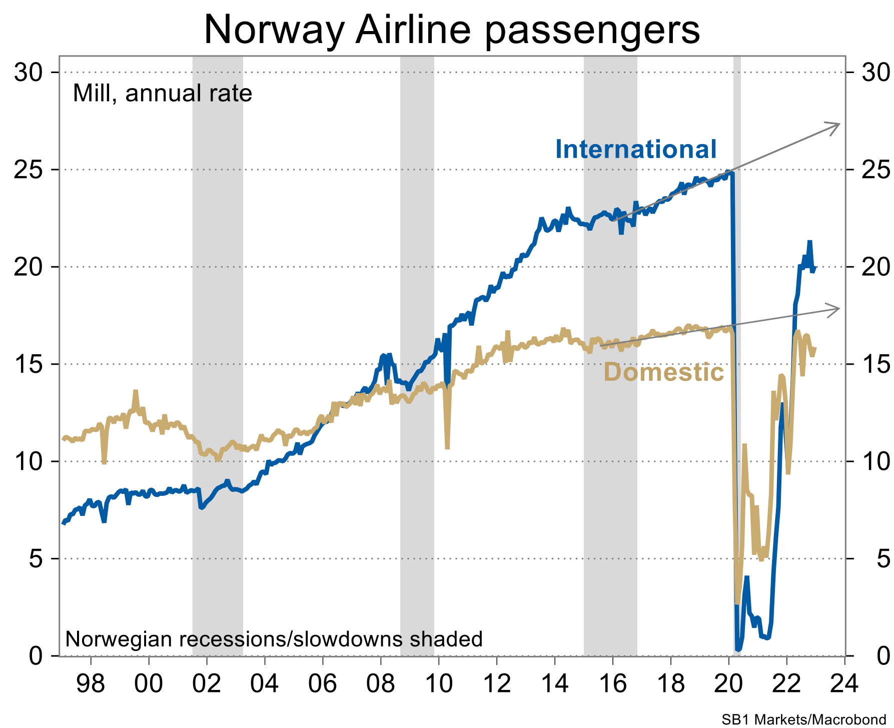
Total no. of passengers down some 12% from the 2019 level. And much lower vs the pre-pandemic trend paths





A Longer term view – this recovery is not complete yet

The uncertainty: How much will business travel behaviour change, permanently?



- International traffic is down 25%+ vs. the pre-pandemic trend path – which was much lower than the pre-2014 growth path
- Domestic traffic was not growing that fast during the 10 years before the pandemic – and the shortfall vs. this trend is less than 10%

Highlights

The world around us

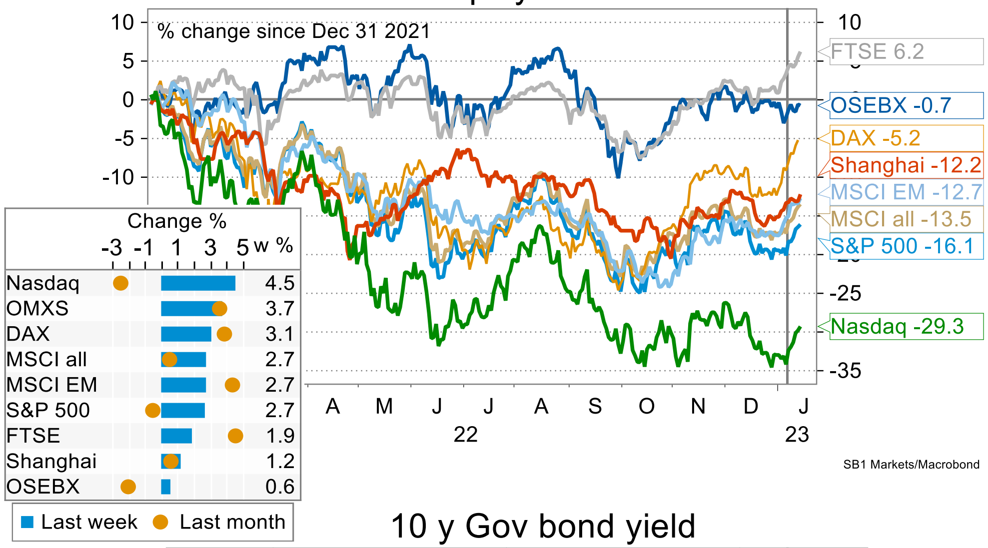
The Norwegian economy

Market charts & comments

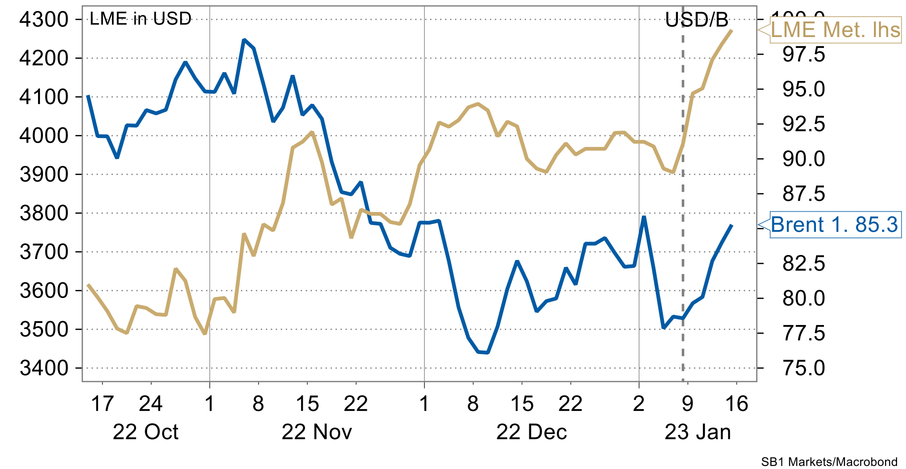
A continued Goldilocks start of the new year: Equities up, bond yields down

Inflation fears are easing – even commodity prices rose (barring European energy prices). The USD down, JPY up

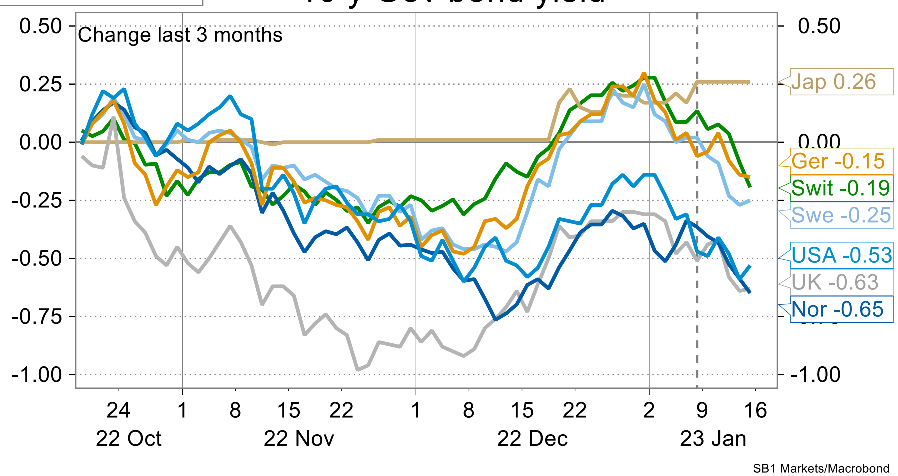
Equity Indices



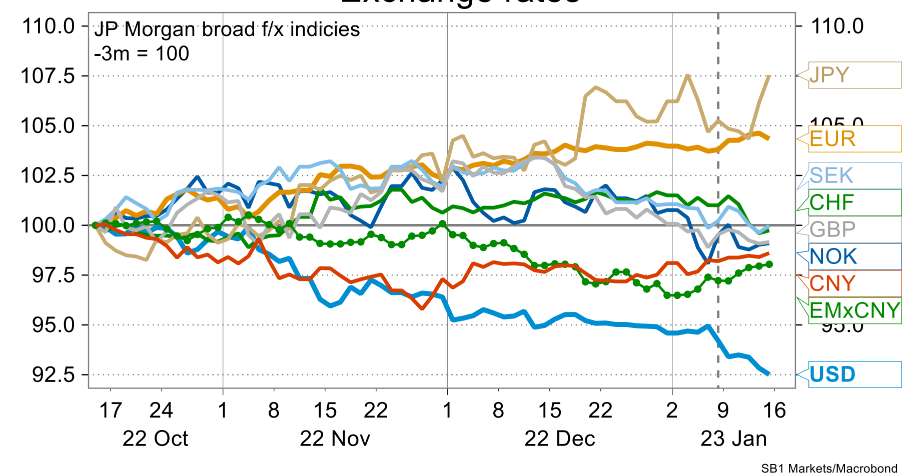
Oil vs. metals



10 y Gov bond yield



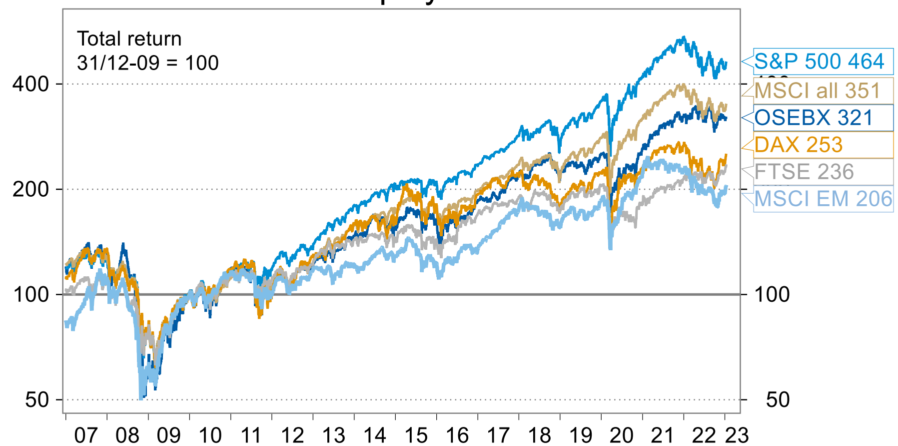
Exchange rates



The long-term picture: Stock markets down, commodities down, yields up

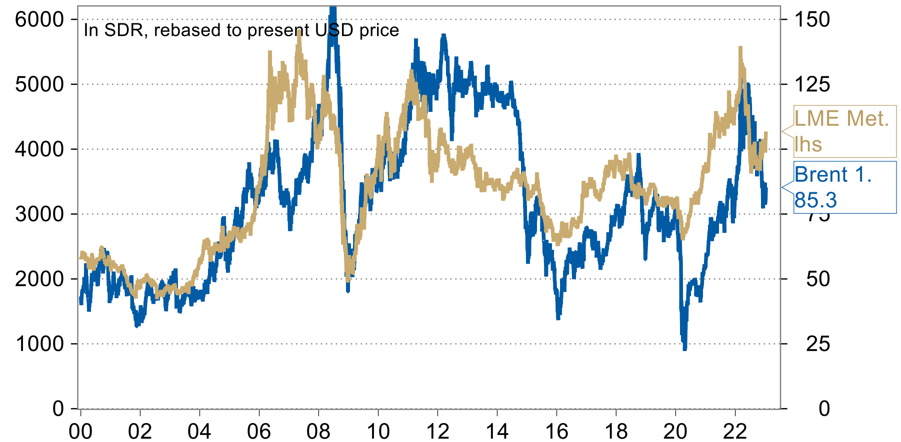
The USD is still strong

Equity Indices



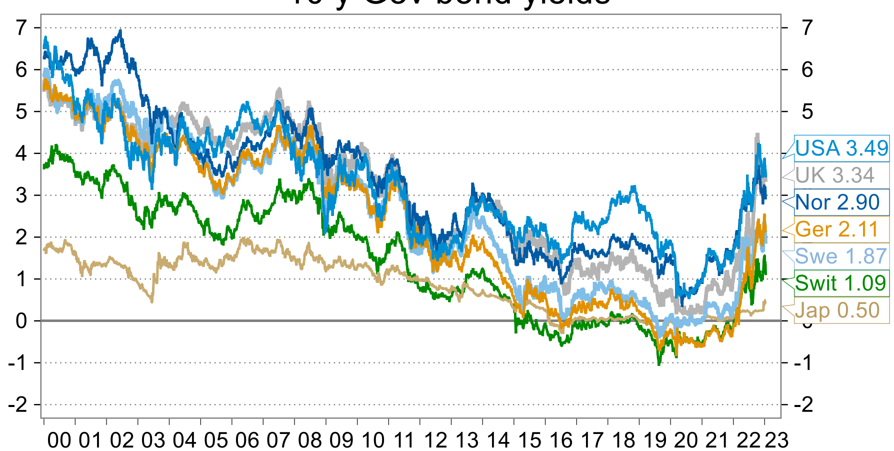
SB1 Markets/Macrobond

Oil vs. metals



SB1 Markets/Macrobond

10 y Gov bond yields



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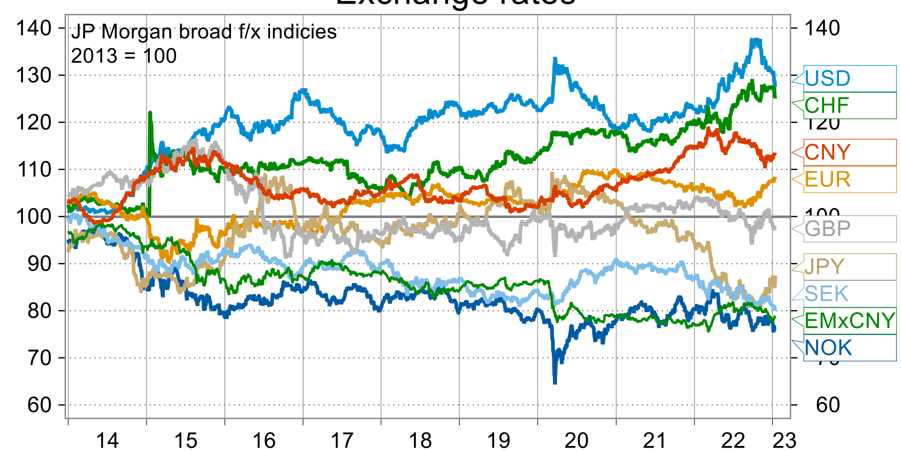
Exchange rates

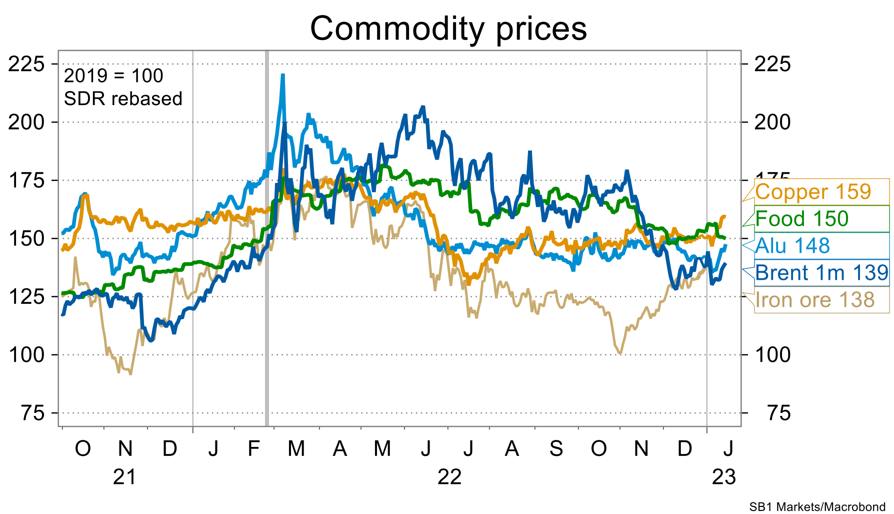


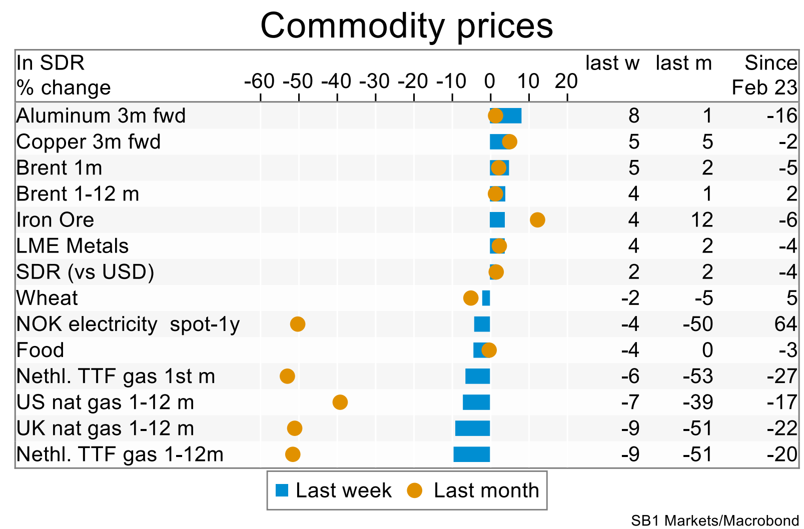
SB1 Markets/Macrobond

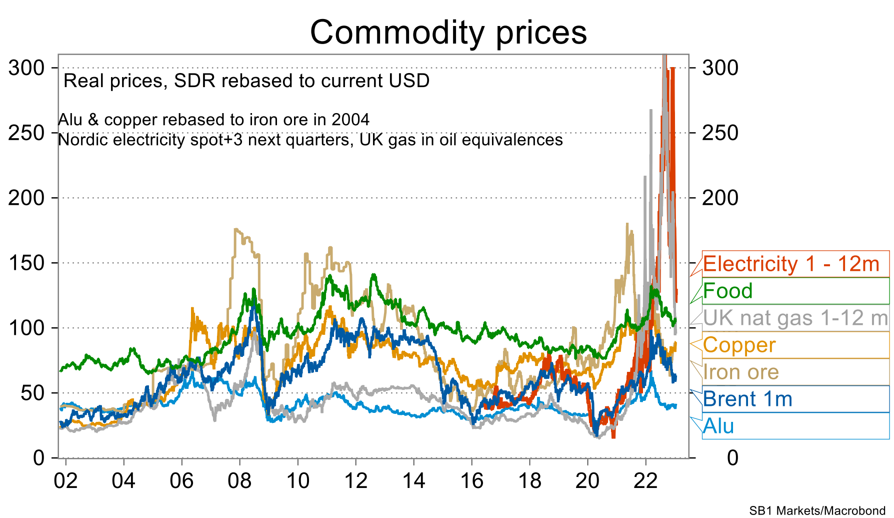
SpareBank 1 MARKETS

Metals/iron ore/oil up on hopes on a strong Chinese reopening recovery

Iron ore prices are climbing further – on hopes of more Chinese demand, post Covid







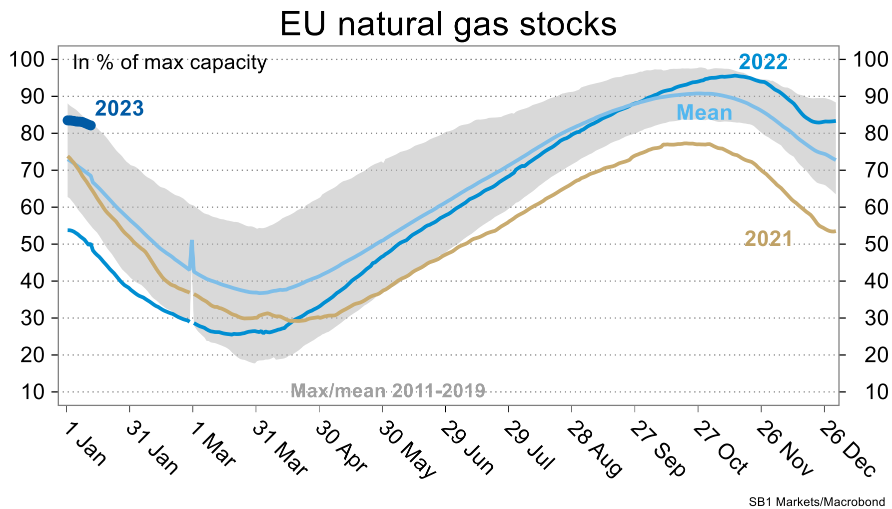
Last week – prices in SDR

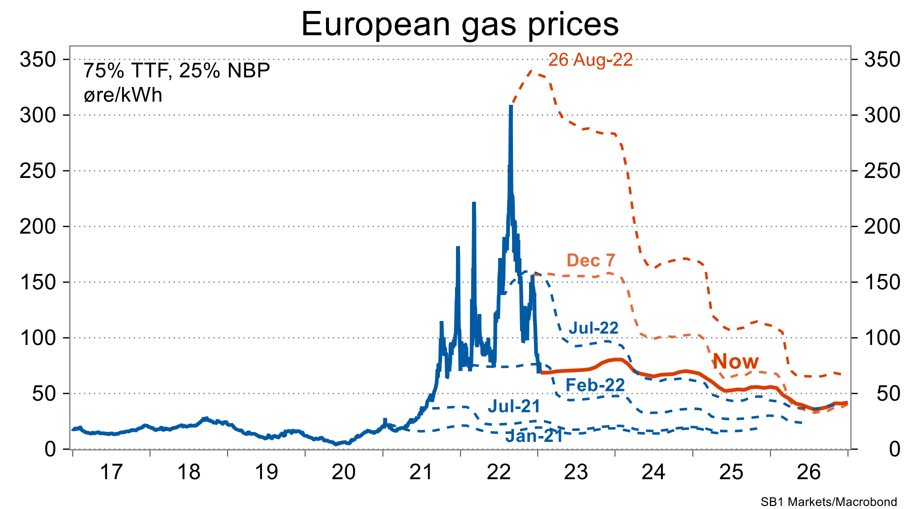
- **Oil prices** up 4% – 5%
- **European natural gas** prices continued downwards by another 6% - 9 %. Since early Dec, prices are halved (for the coming 12 months!). Spot prices are lower than before the war started. If the market is right (now), a substantial impact on European inflation the coming months and through 2023
- **Iron ore** prices have recovered sharply since early November on hopes for a recovery in the Chinese construction sector following scrapping of Covid restrictions and stimulus measures, and rose further last week
- **Other metal** followed suit last week
- **Food prices** fell, are flat m/m – and lower than before the war started

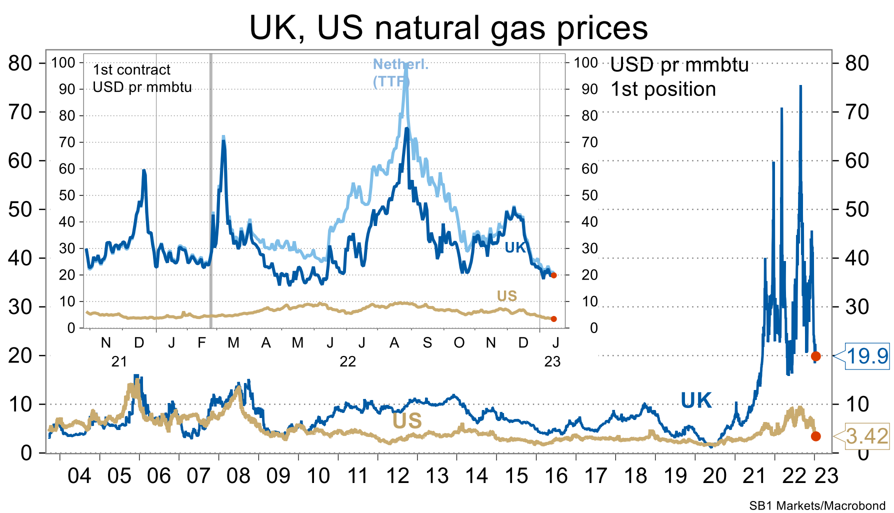
SpareBank 1 MARKETS

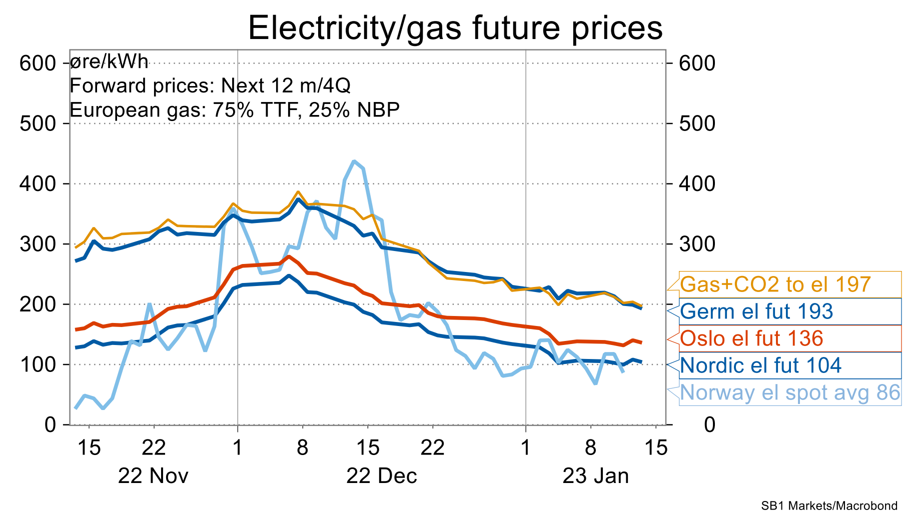
European gas stocks soon the highest ever? Prices keep falling

2023 prices cut in half since early December



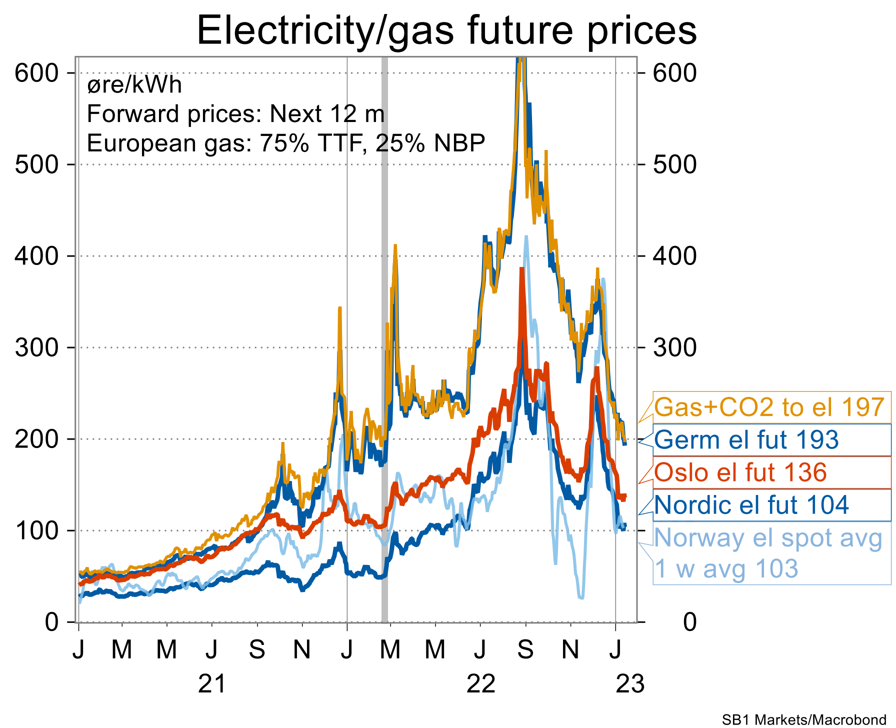


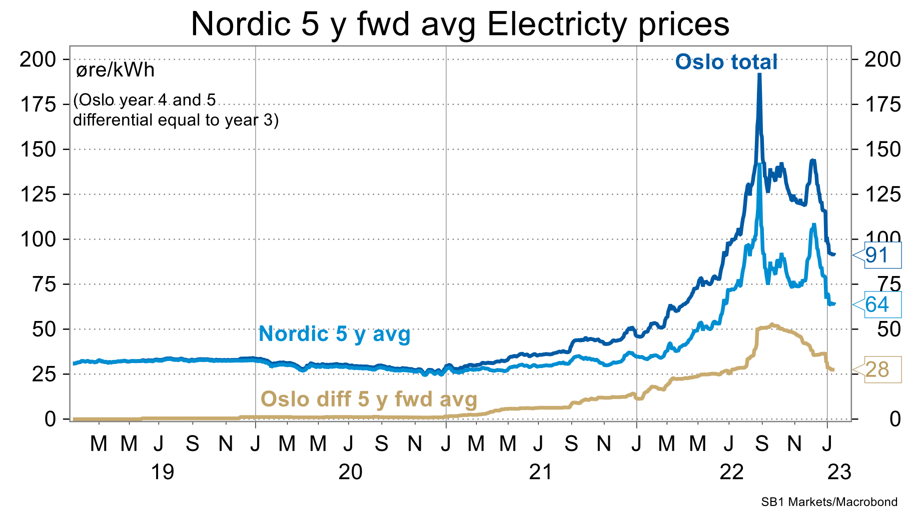


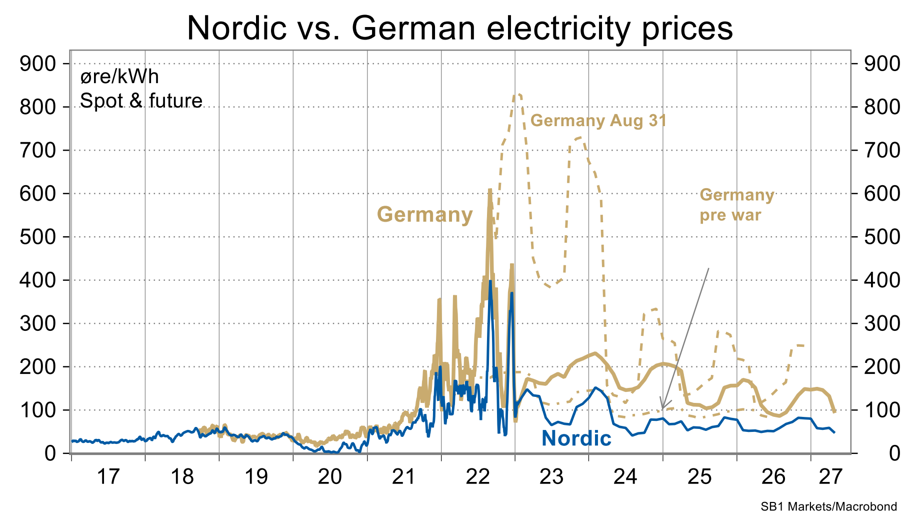


European gas/el. prices are still high, but far less than feared short time ago

Spot prices are lower than before the war started but future prices remain significantly higher

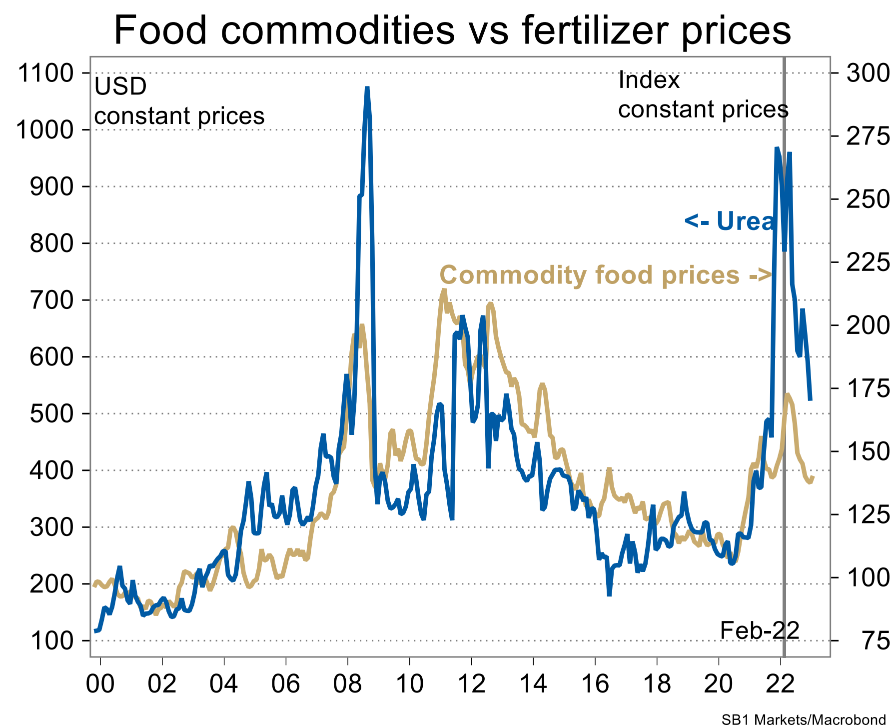


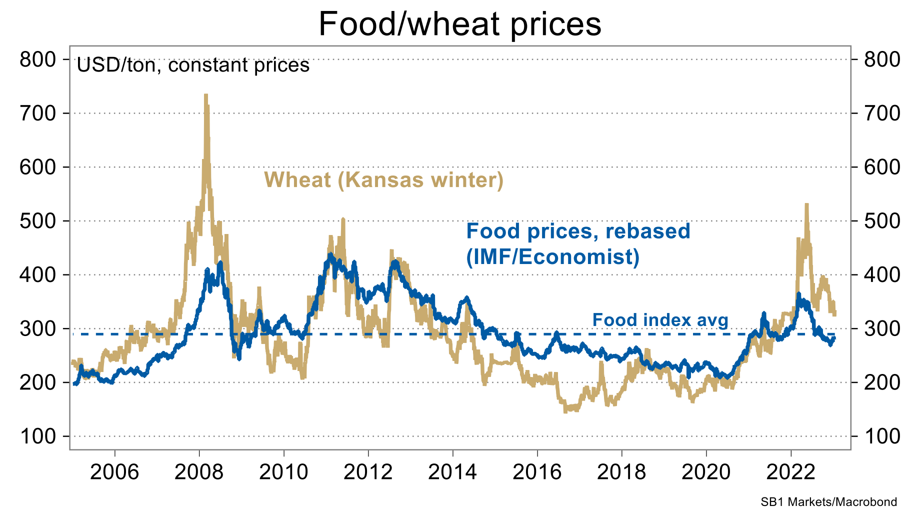


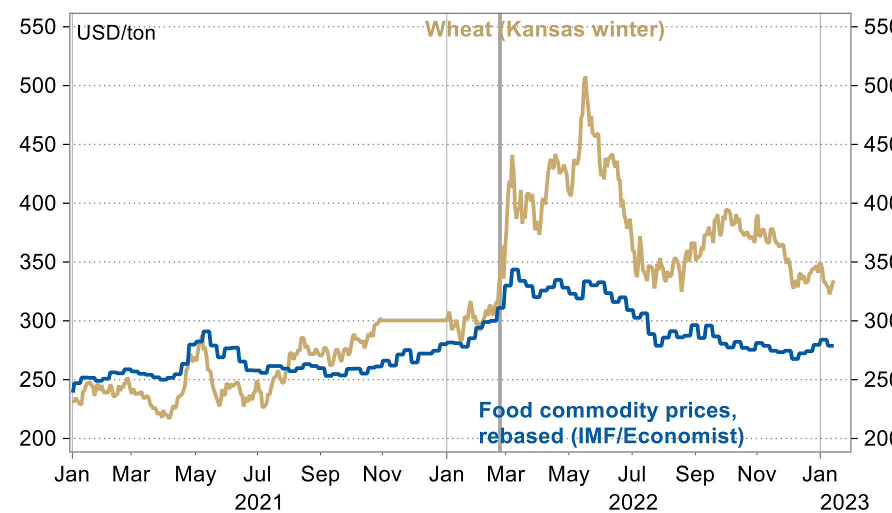


Food prices are trending down, and fell last week

The real price level is not that high, *and below the 10 y average*. *A global food crisis??*



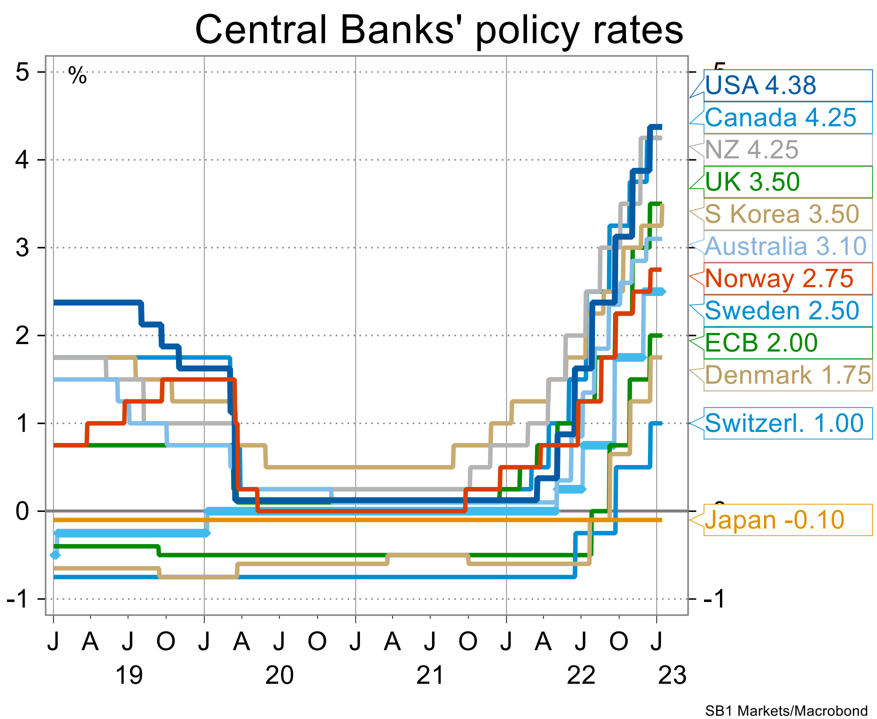


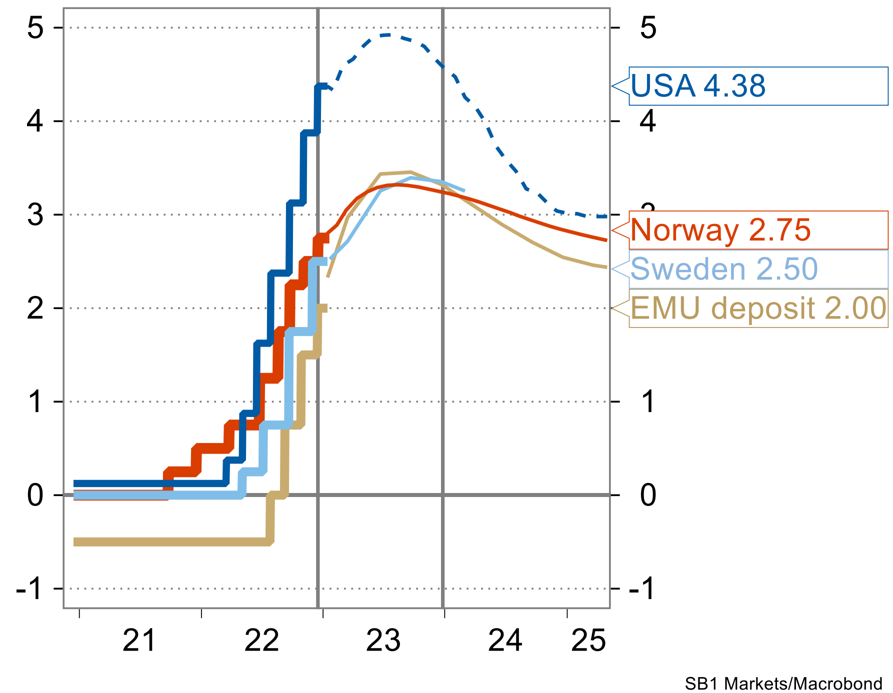


- Urea prices have come sharply down to, since early 2022 – but prices remain higher than normal

South Korea continued with a 25-bps hike

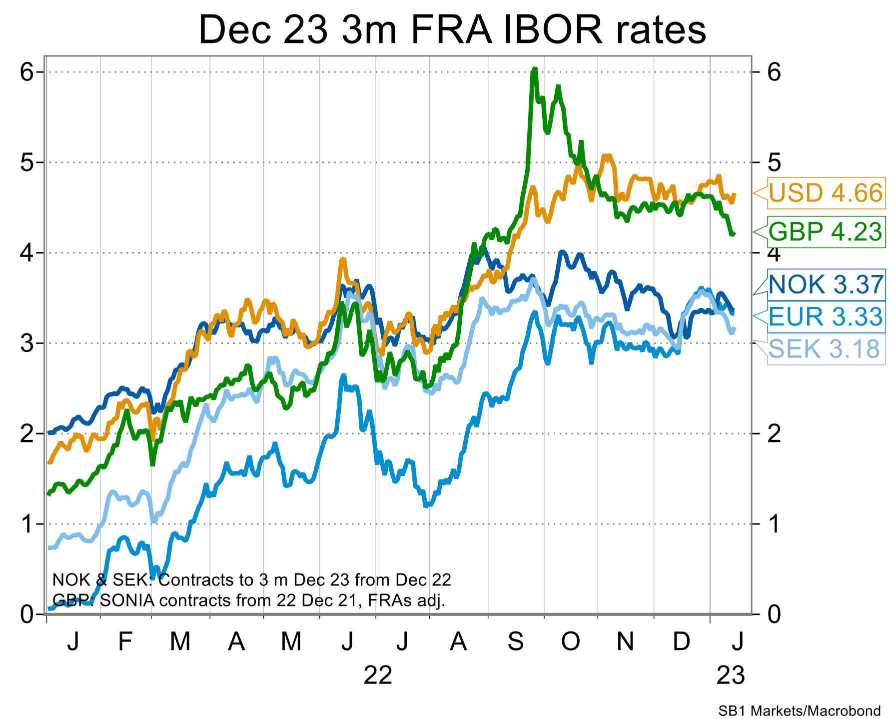
Both the Riksbank and ECB (as well as the BoE) are still expected to hike to a higher level than Norges Bank

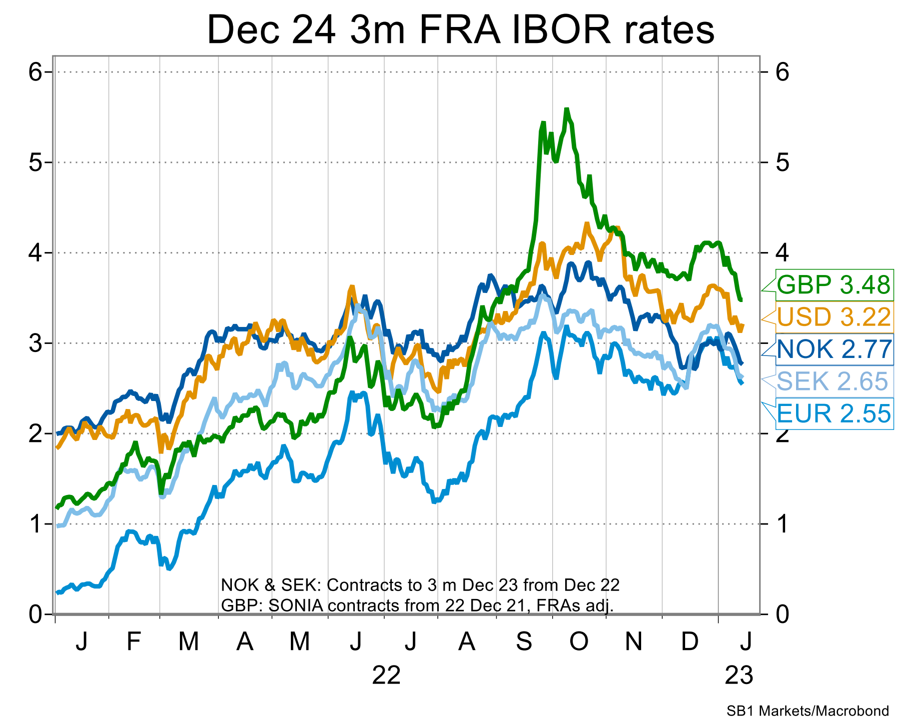




Market expectations further down last week – on upbeat inflation news

GBP and NOK FRA rates declined the most, USD rates the least (and by just 1 bps in 3m Dec 23)

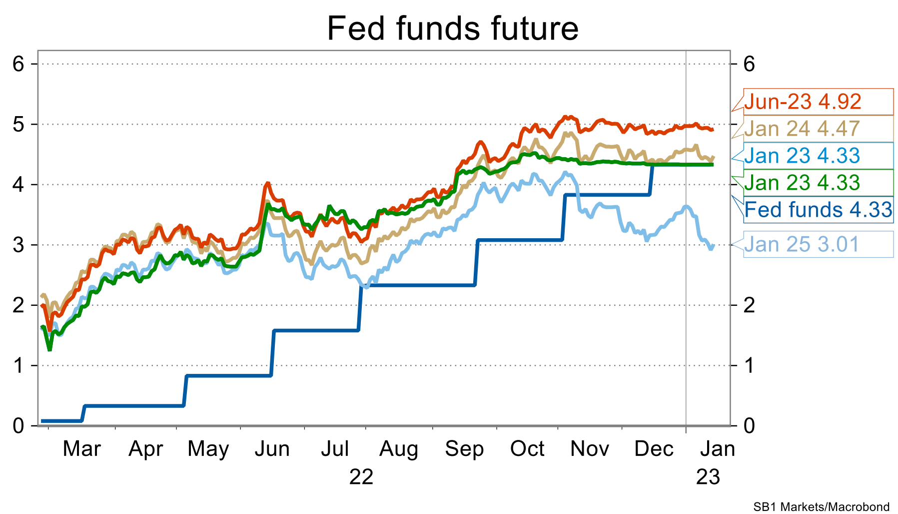


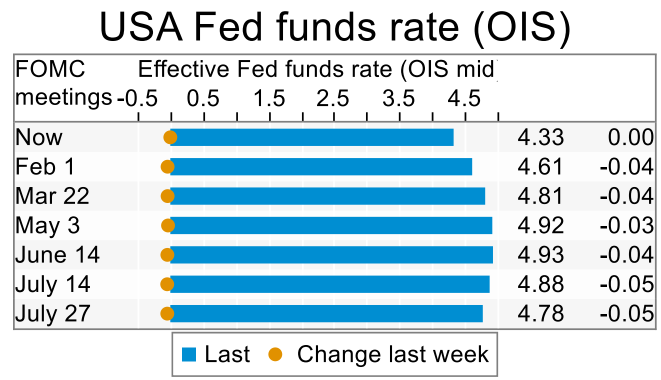


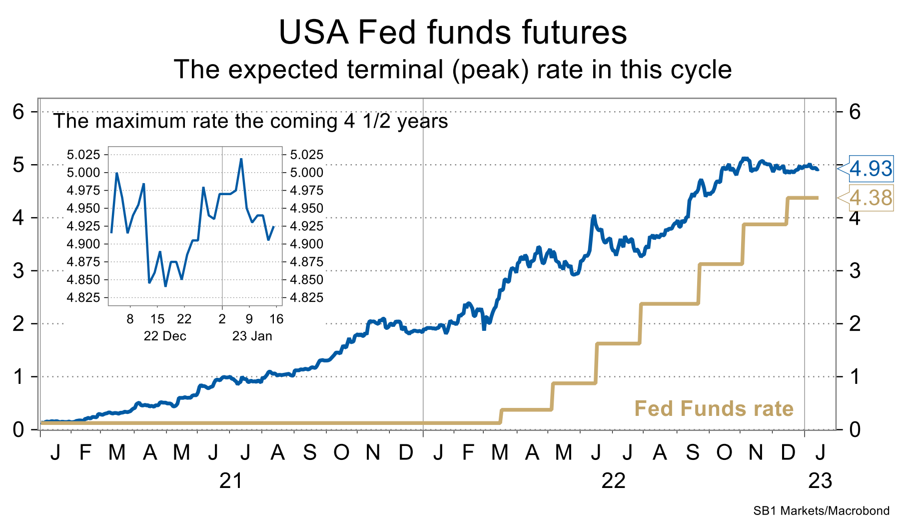
- **Dec-24 FRA** rates fell more then Dec-23, rather naturally

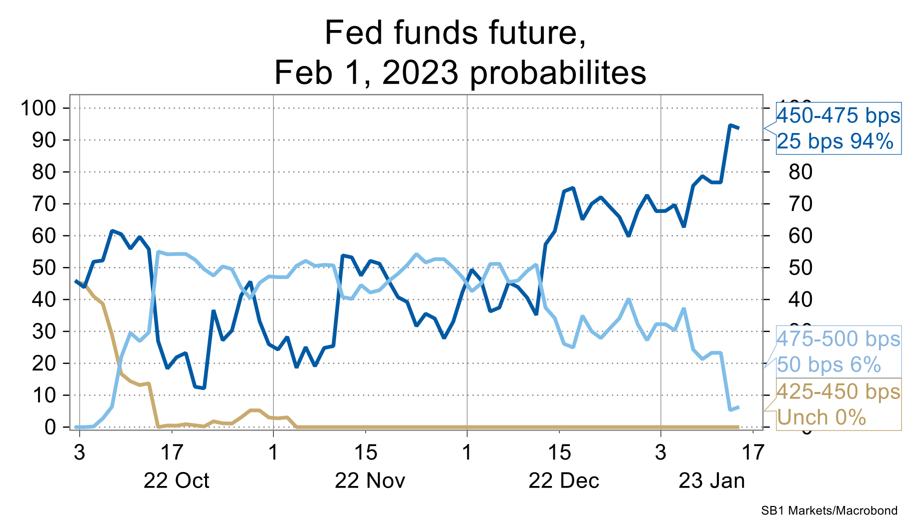
Rate expectations just slightly down in the short end of the curve

25 bps in February a done deal: The probability for a 25 bps hike in early rose to 94% from 74% last week



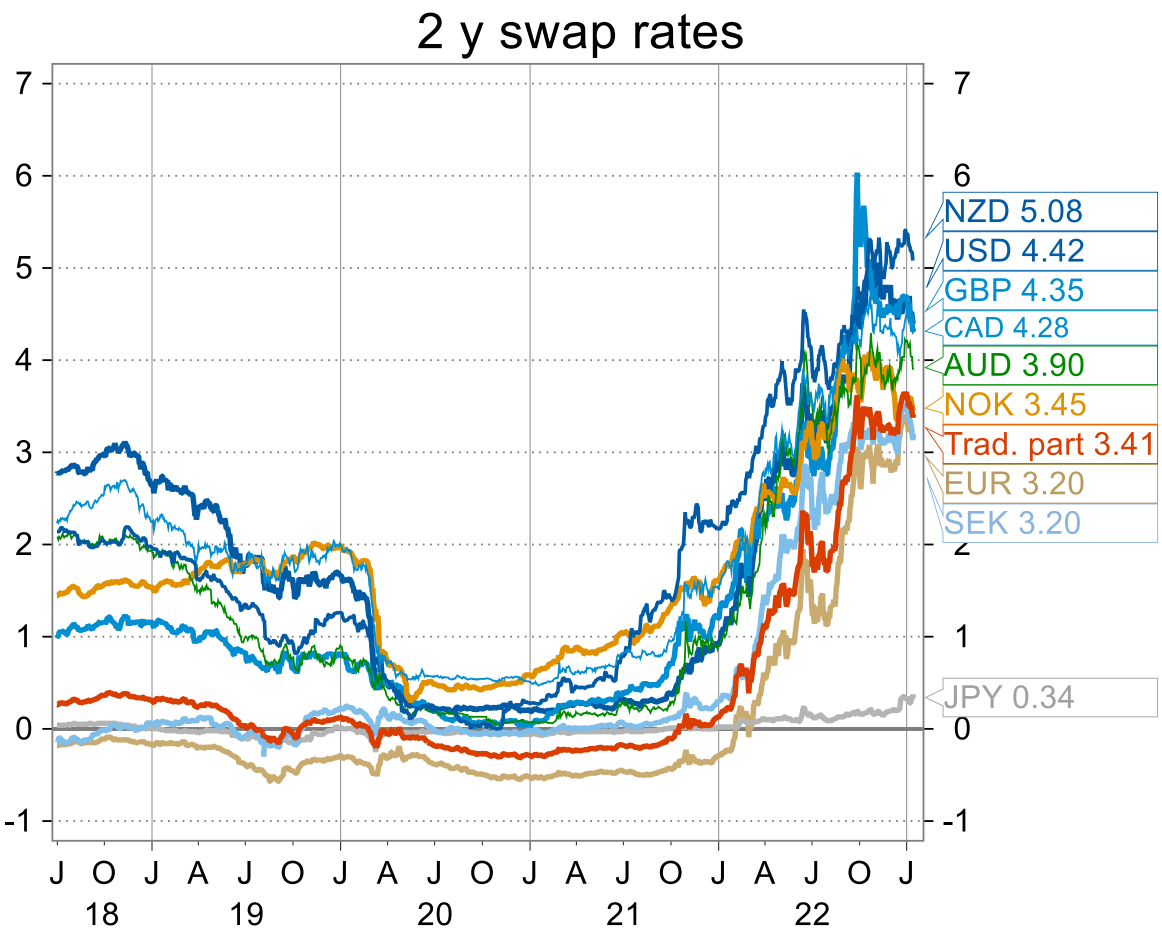




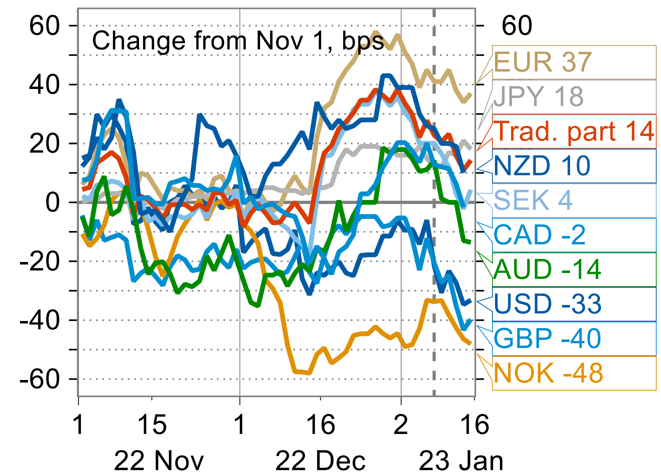


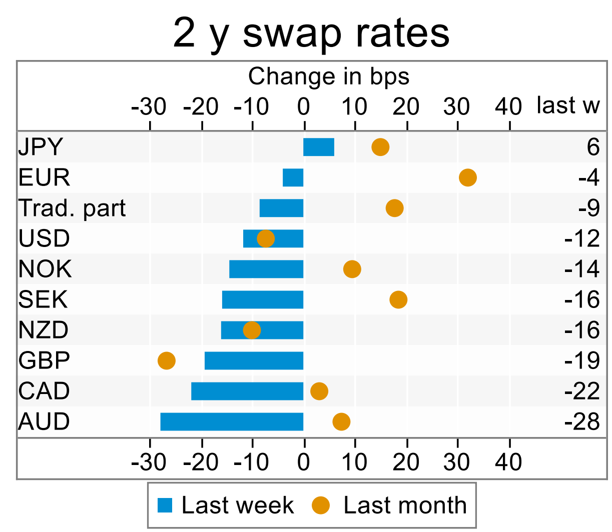
SpareBank 1 MARKETS

2 y swaps down everywhere, and by the least in EUR & USD



SB1 Markets/Macrobond





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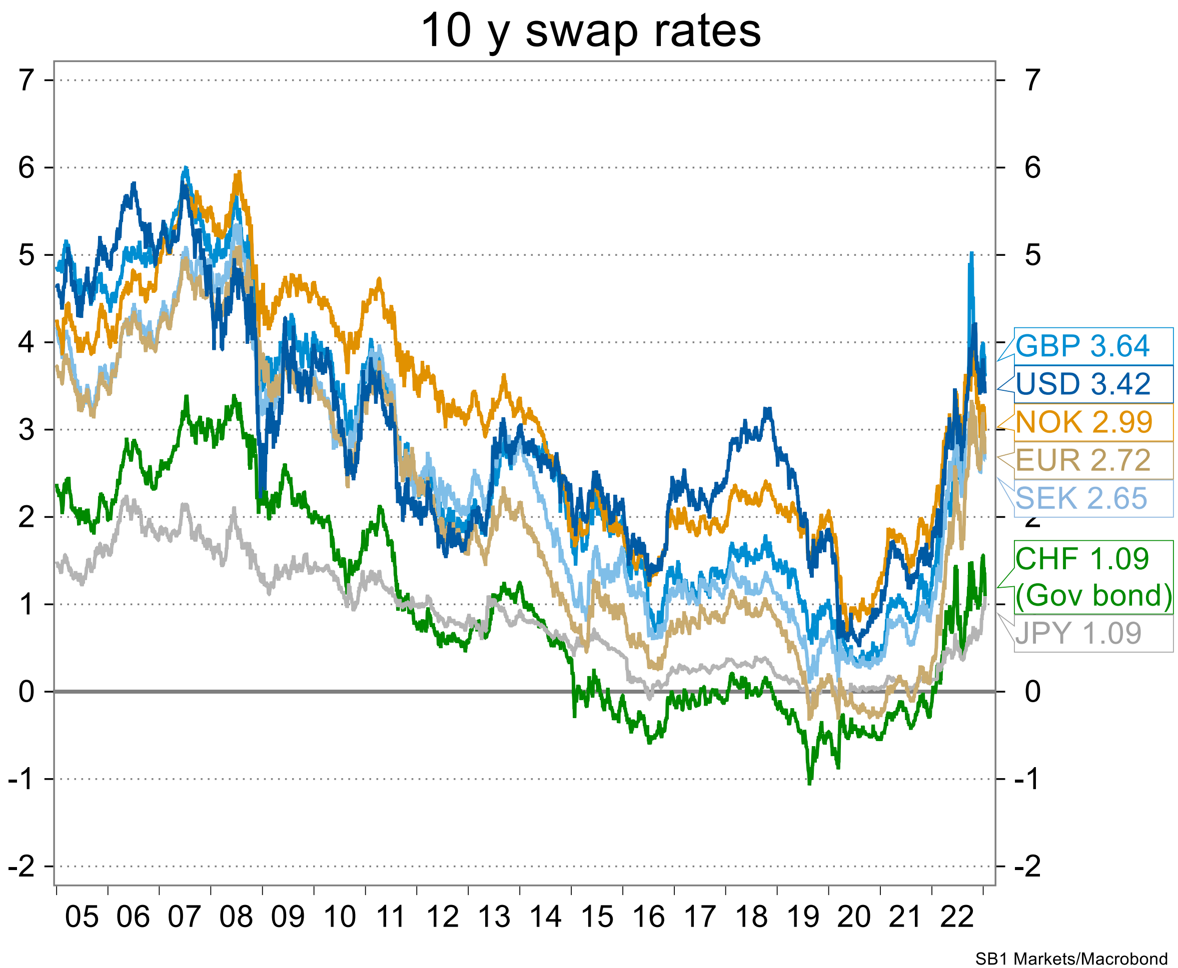
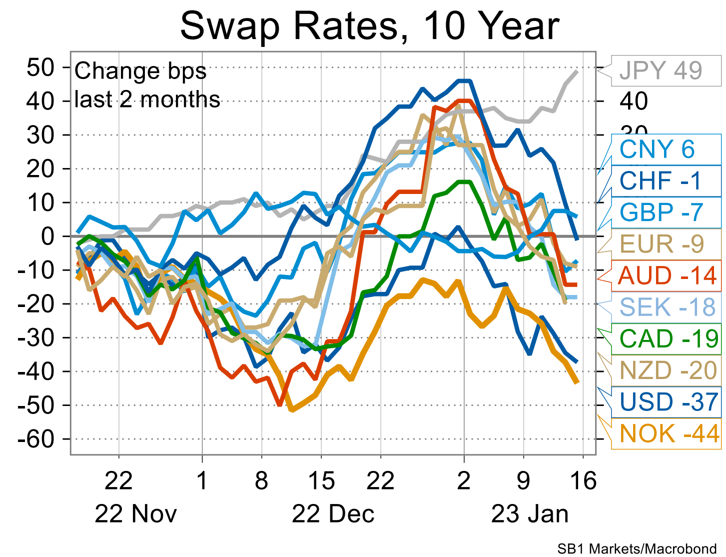
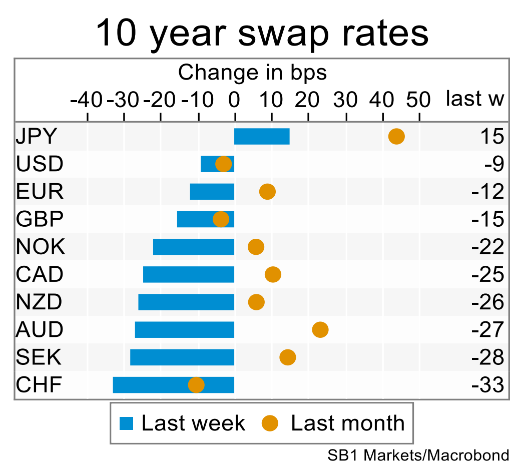
The long end of the curve down everywhere, except for Japan

A large decline on hopes for lower inflation

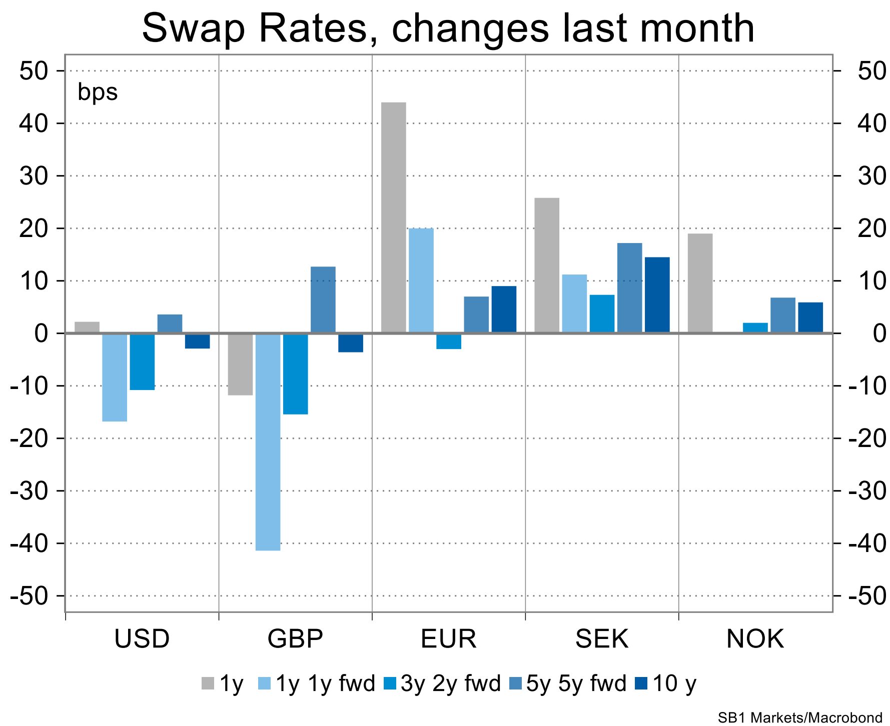


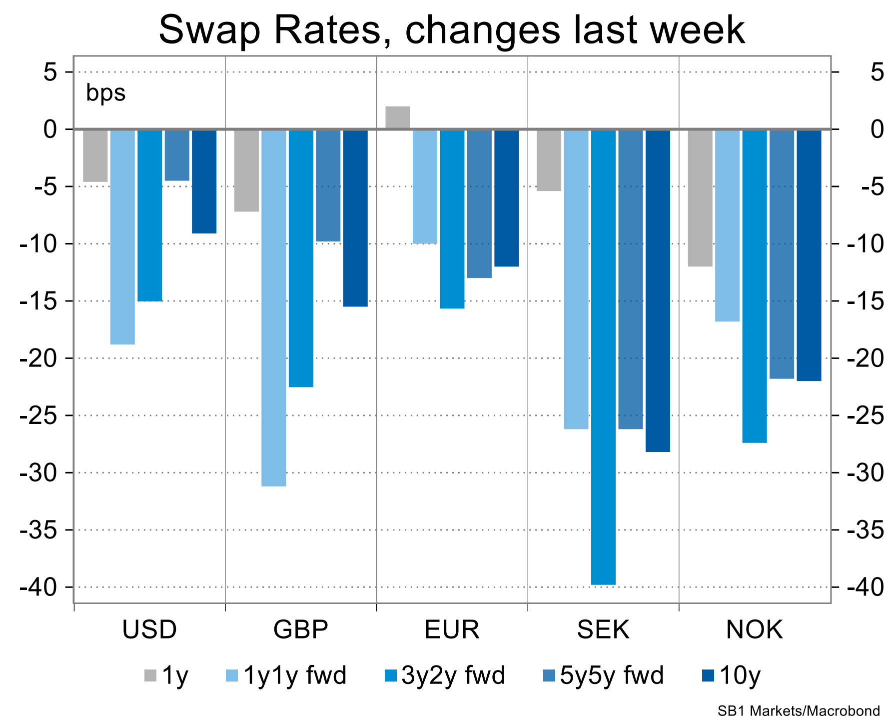




A solid decline in most yield curves last week, NOK and SEK in the front end

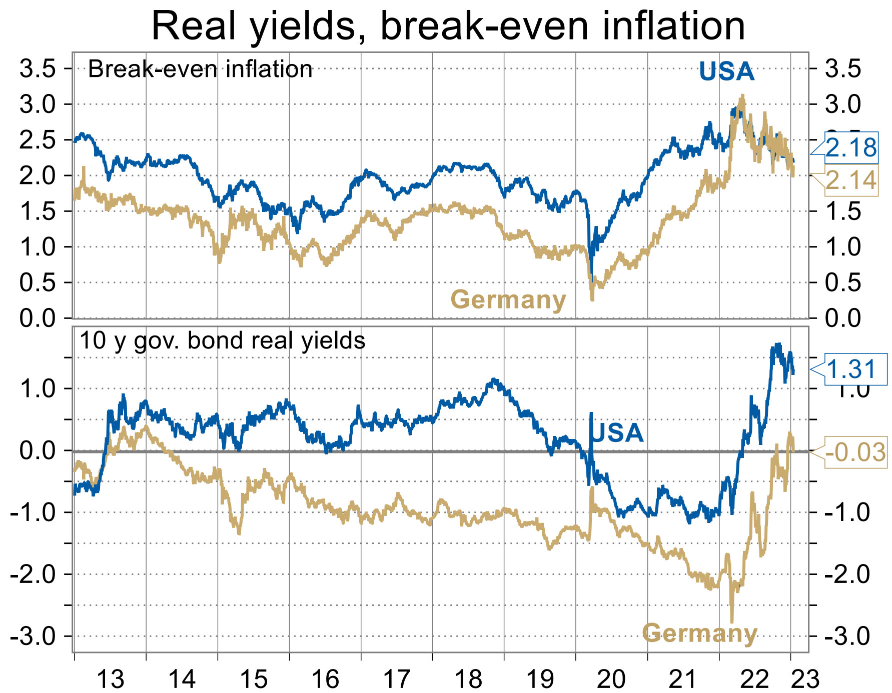
Rates are still mixed vs. one month ago – the most are up, especially the short end in EUR

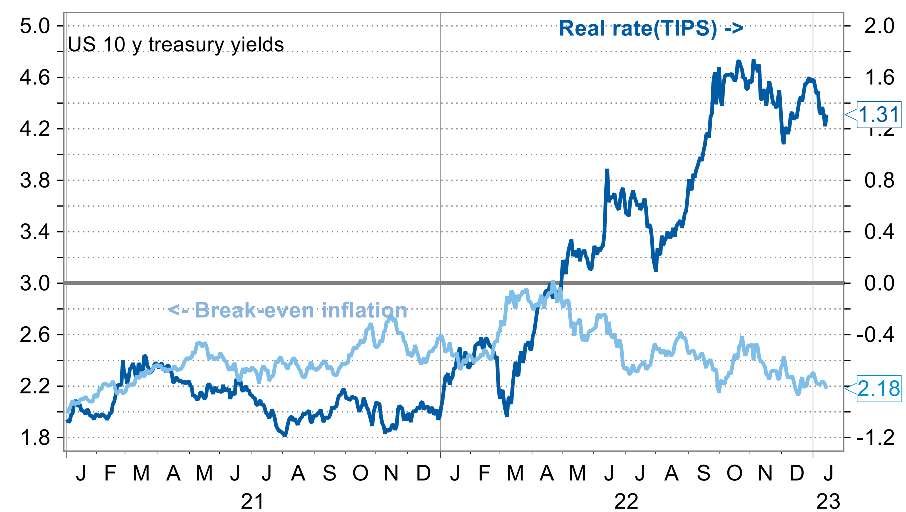




Small changes in US rates, real rates in Germany down to below zero again

US real rates have been trending down from the 1.7% peak in November. Inflation expectations since early 2022





- In the US, a 10 y CPI expectation at 2.14% is marginally below Fed's 2% target for the PCE-deflator (which on average is some 0.3 pp below CPI inflation). Our model have for some weeks suggested that the break-even inflation component was too high. Now, the gap is almost closed
- The German y break-even drifted down too, but rose last week. The 10 y real rate turned negative again but the trend is still upwards, from very low levels

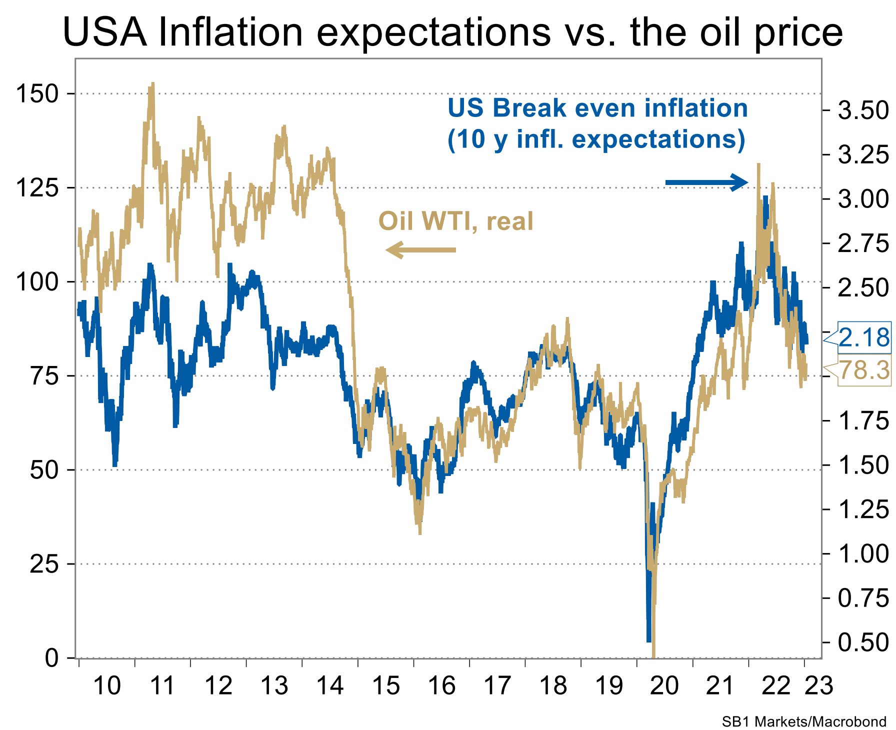
US & Germany 10 y Gov bond yield

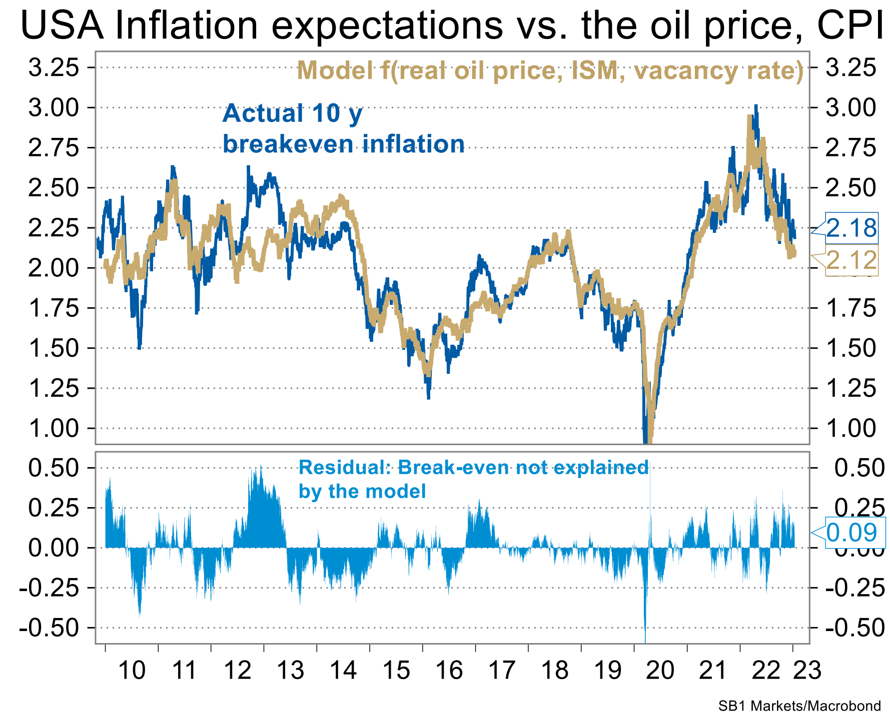
	Yield	Change 1w	Change 1m	YTD	Min since April-20
USA nominal treasury	3.49	-0.06	-0.02	-0.39	0.52
.. break-even inflation	2.18	-0.03	-0.06	-0.12	1.06
.. TIPS real rate	1.31	-0.03	0.04	-0.27	-1.19
Germany nominal bund	2.11	-0.09	0.22	-0.45	-0.64
.. break-even inflation	2.14	0.11	-0.11	-0.15	0.42
.. real rate	-0.03	-0.20	0.33	-0.30	-2.80

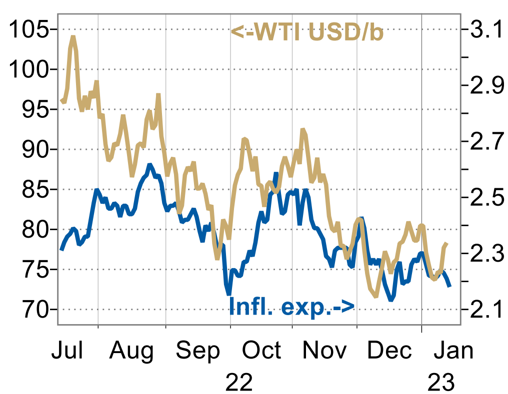
SB1 Markets/Macrobond

US inflation expect. down – and now needs some support to get further down

The current break-even is just 9 bps above our model current f'cast (based on the oil price, ISM & the vacancy rate)

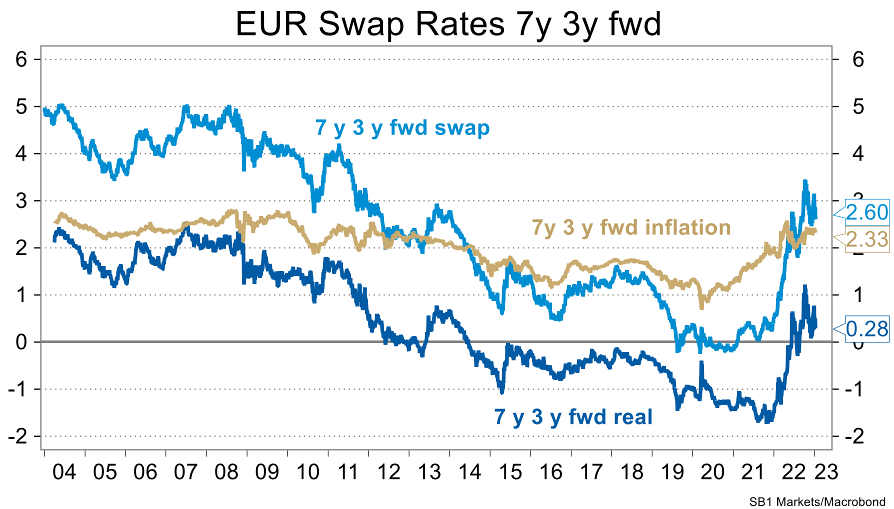


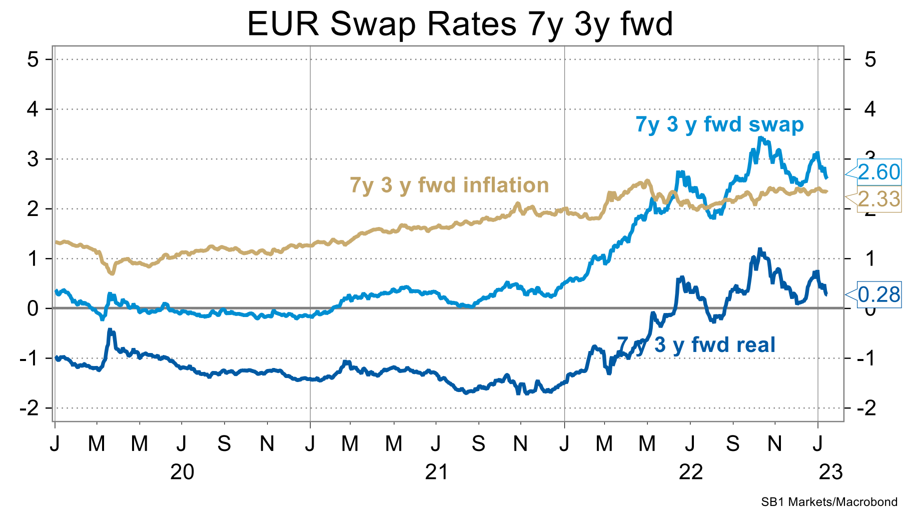


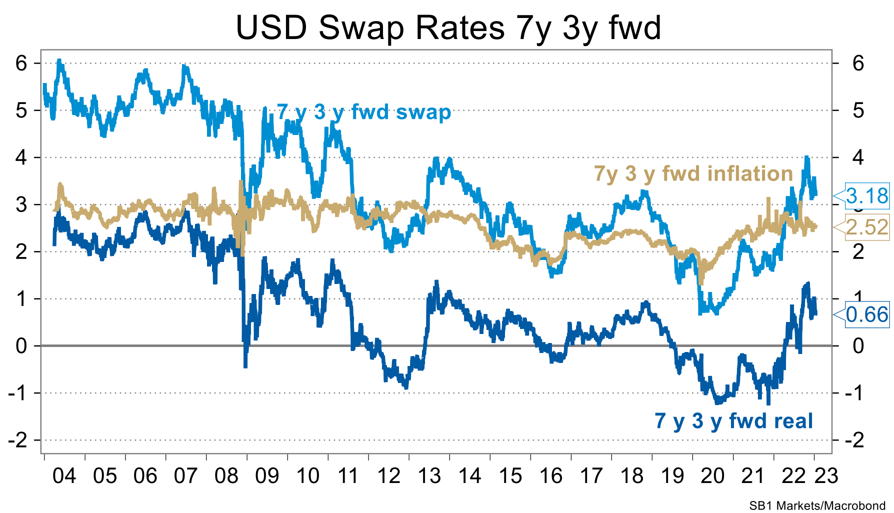


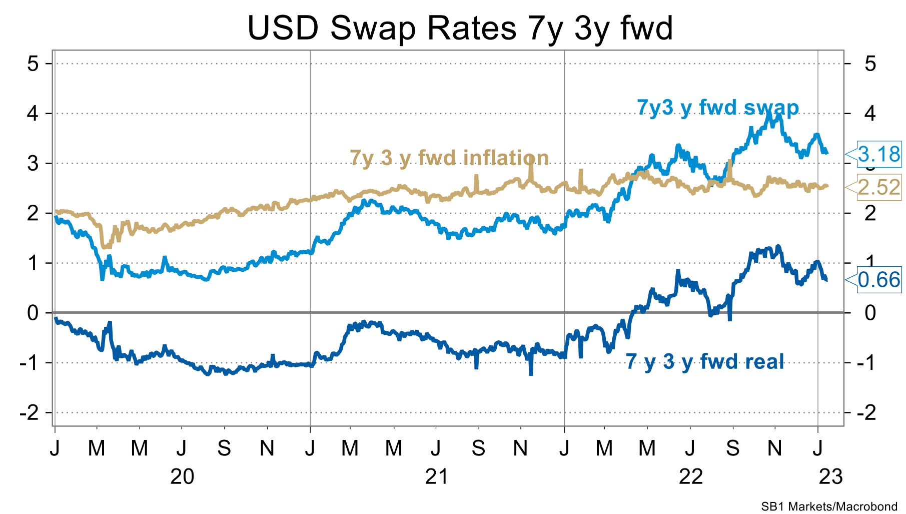
- A simple model including the <u>spot</u> oil price, the <u>current</u> ISM and the <u>current</u> vacancy rate pretty well explains the <u>long-term</u> breakeven inflation expectation in the bond yield curve
- What now? The actual break-even is in line with the model forecast. We are uncertain about the oil price, but rather confident that both the ISM, and the vacancy rate will decline. Impact vs the 10 y break-even expected inflation rate:
  - -5 ISM points: -12 bps
  - -3 vacancy pts, (to 3.2% from 6.2%): -36 bps
  - - 10 USD/b: -10 bps

European real (swap) rates also down last week



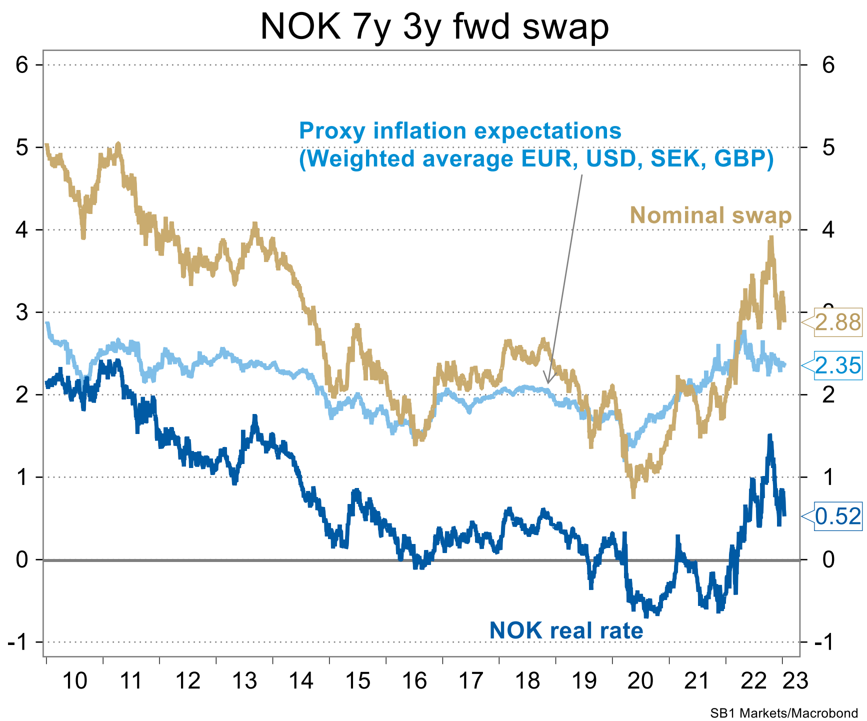


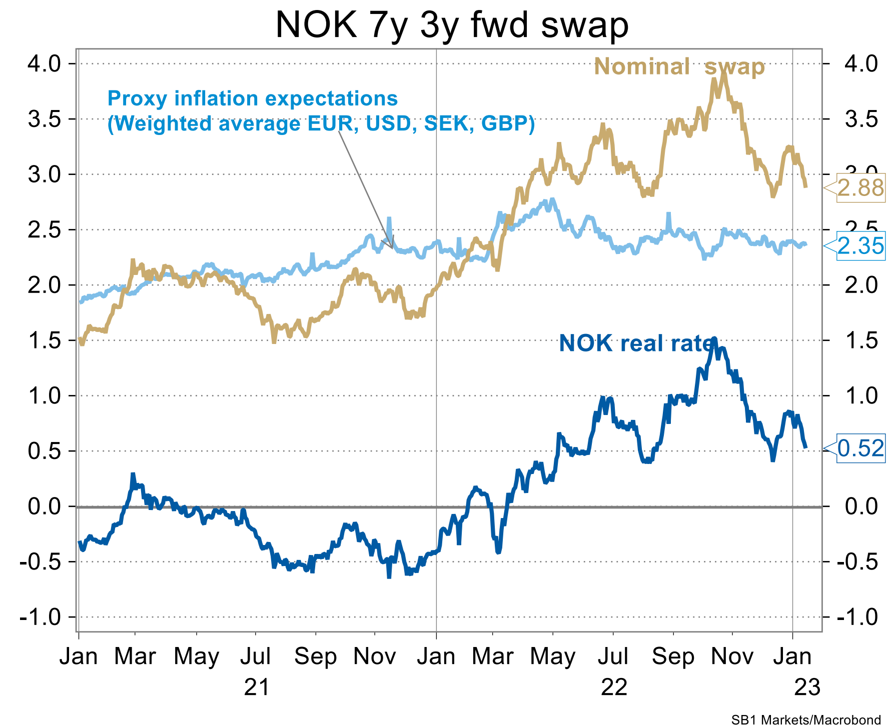


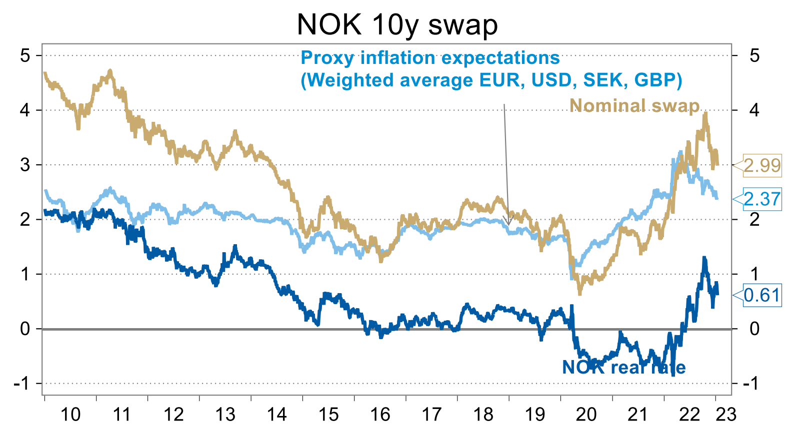


NOK real rates also sharply down last week

… as the decline in nominal swap rate was much smaller than abroad



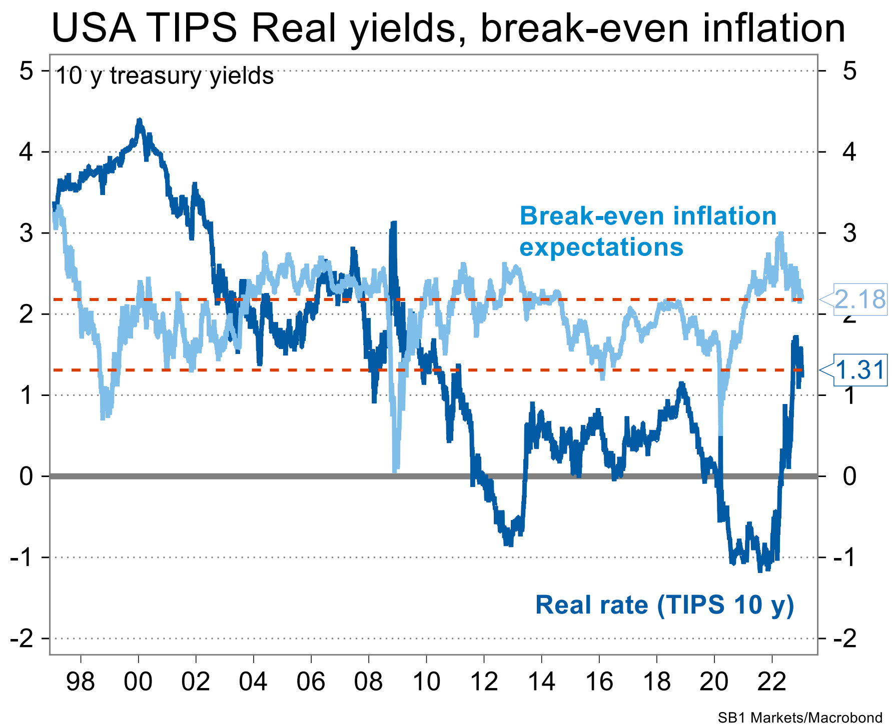


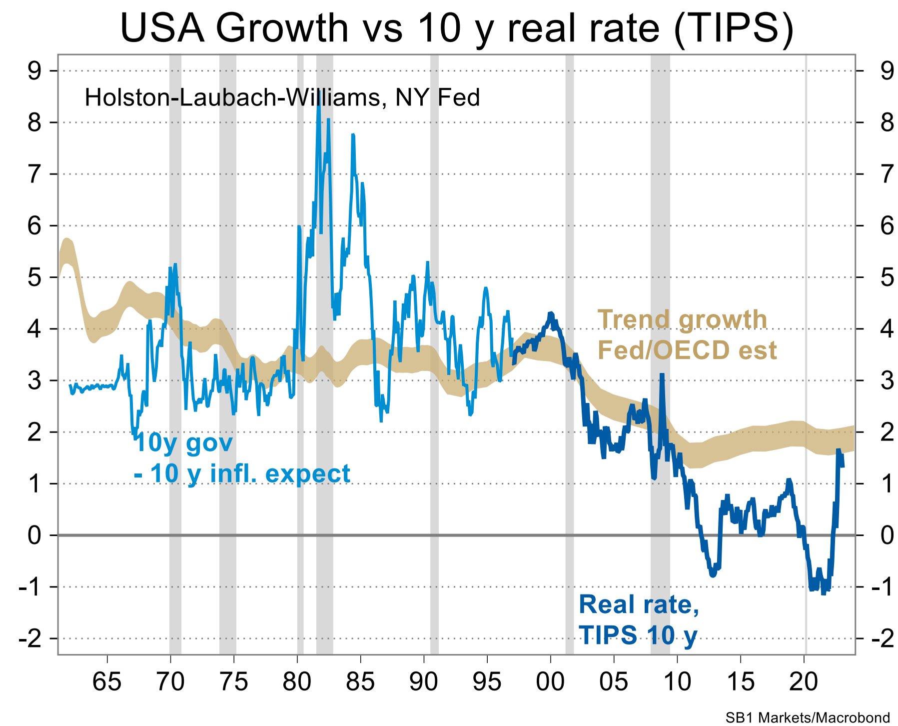


Memo: Our NOK inflation expectation proxy is a weighted average of EUR, SEK, GBP, and USD inflation swaps, cross-checked vs historical inflation differentials and inflation expectations from surveys

Growth vs real rates: Real rates on the low side but not by much

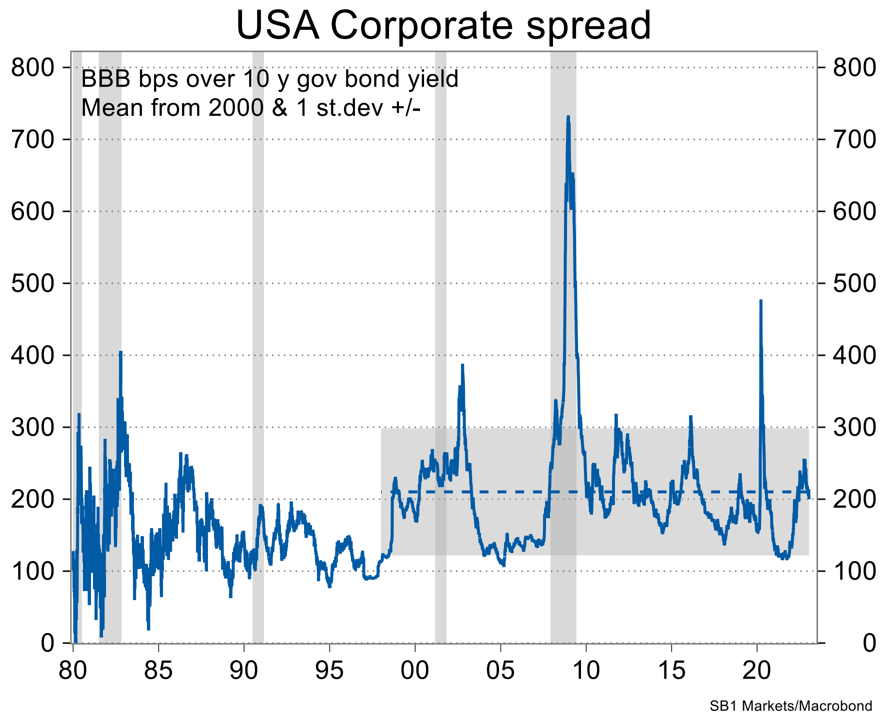
At least not compared to the differential during the pandemic

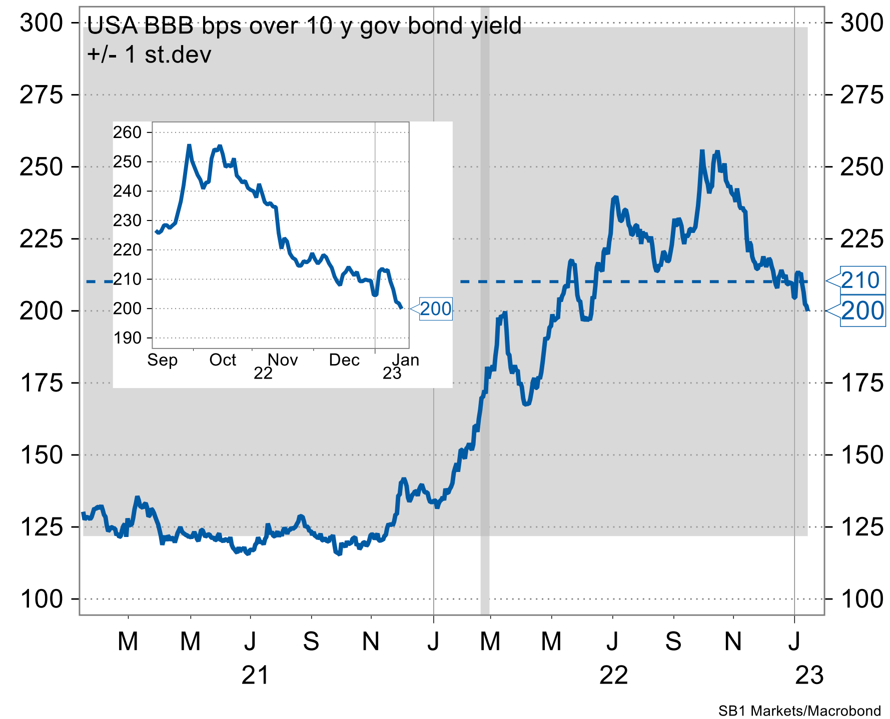




Risk on: Credit spreads down again

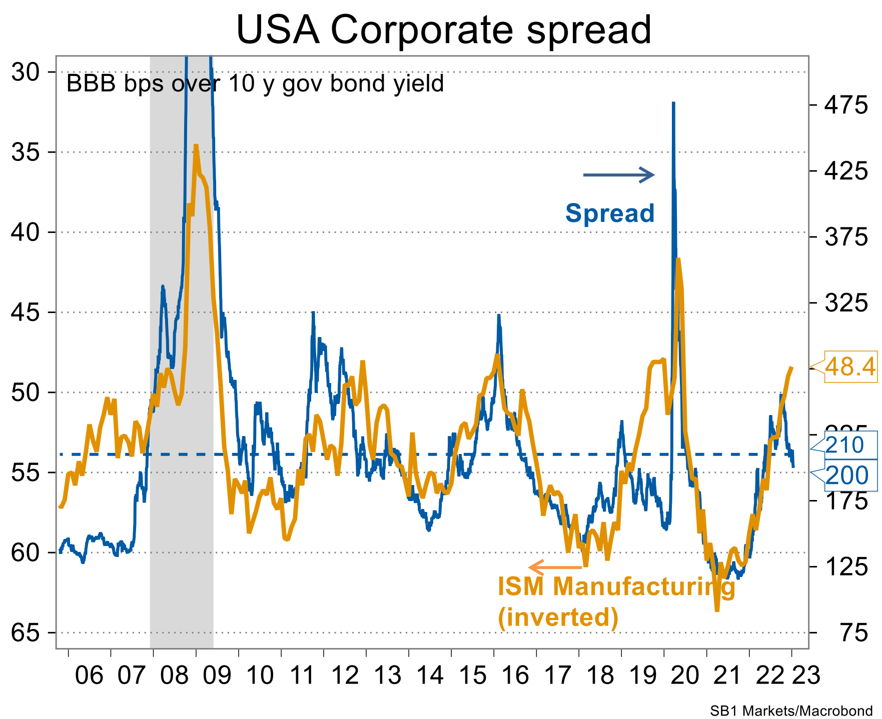
Even so, we think the spreads are exposed to a weakening economy

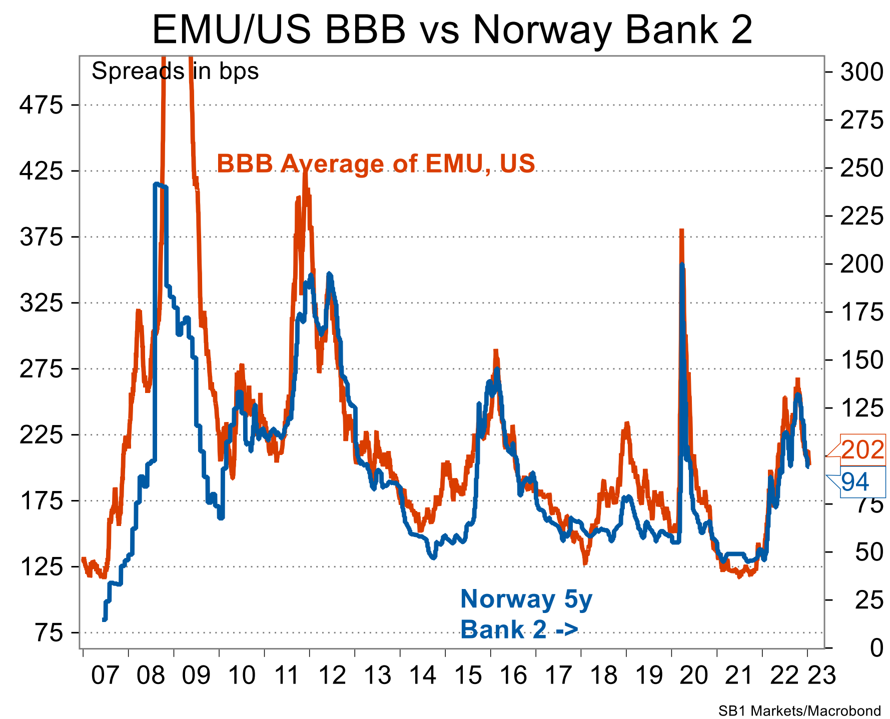




Mind a new gap: The economy is weakening (ISM), and spreads are narrowing

What do you think is more likely: An ISM at 45 or 55 before summer? We are quite sure, it's at 48 already

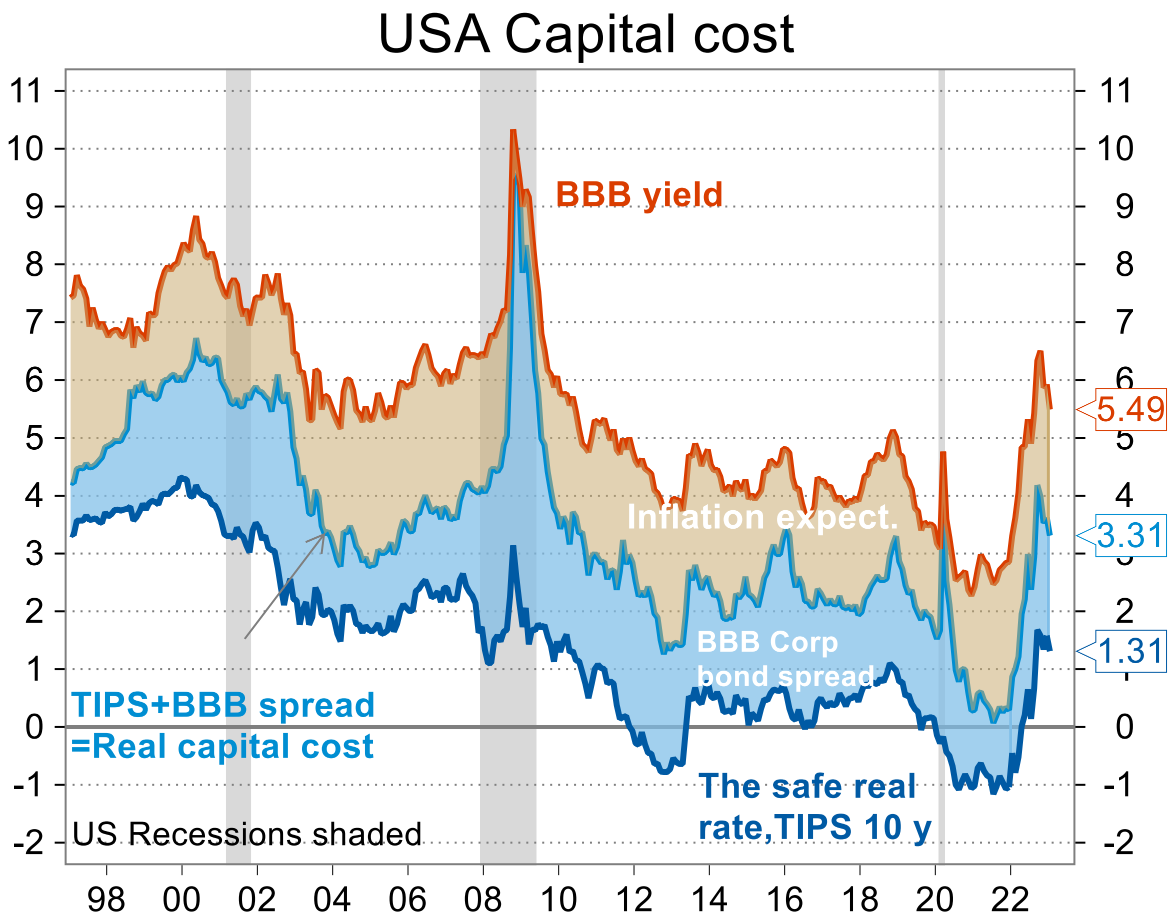




- Last week: Norwegian credit spreads flattened – but the trend is flatly down

The cost of capital is still higher than in more than a decade

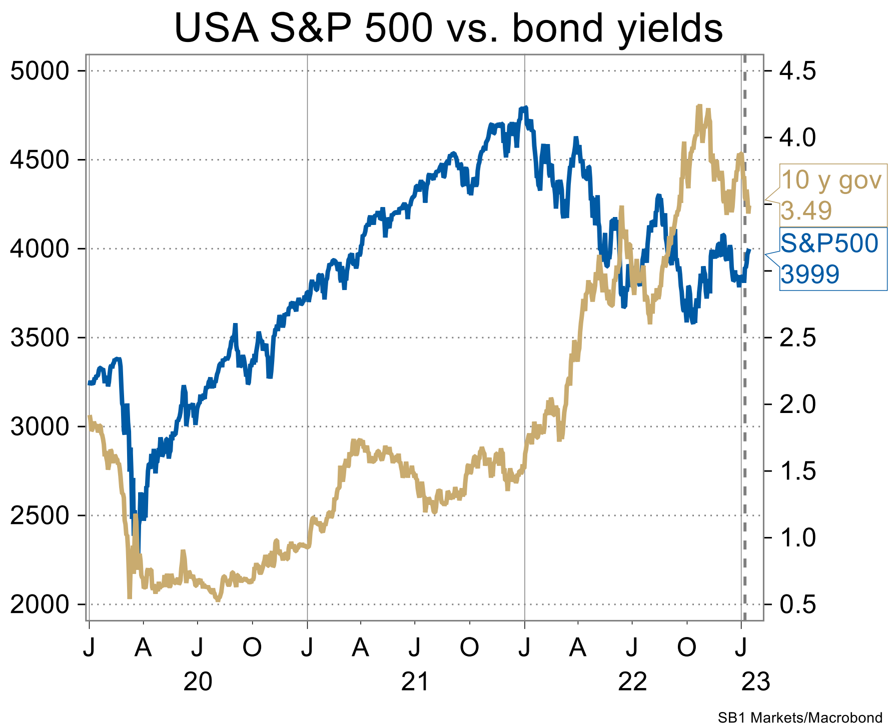
All valuation metrics have changed dramatically. *As have all calculations of return on capital*

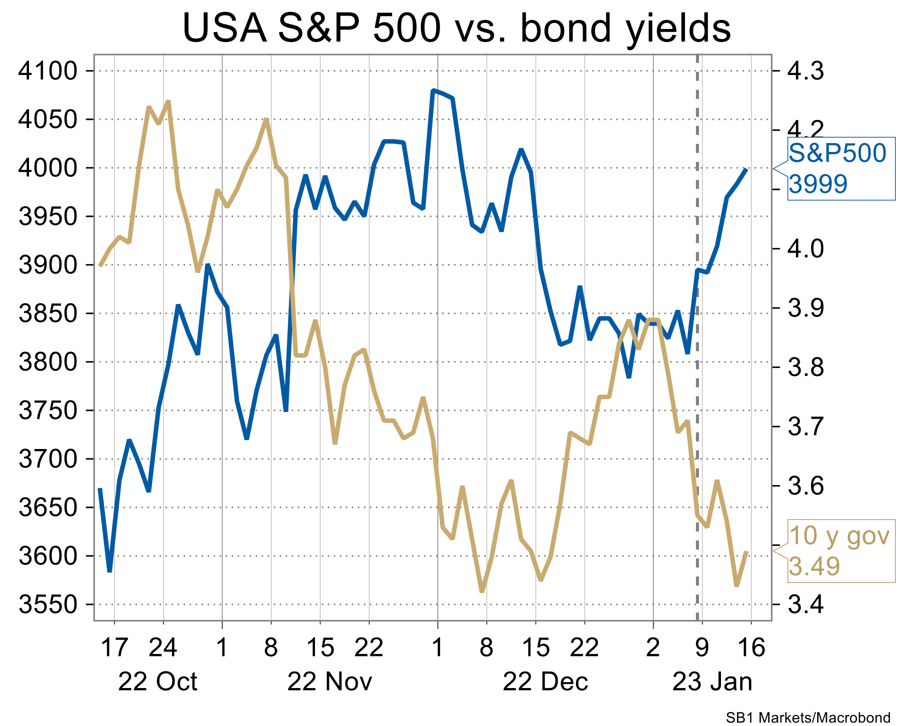


SB1 Markets/Macrobond

- **Spreads** flattened last week
- The total real borrowing cost for a BBB company has increased to 3.3% bps from zero by the end of last year:
  - The TIPS real rate is up from -100 to + 131 bps
  - The BBB corporate investment grade spread is up from 120 bps to 213 bps
- Add on modest inflation expectations, the nominal borrowing cost has increased from well below 3% to 5.7% (though down from 6.7% at the local peak last October)

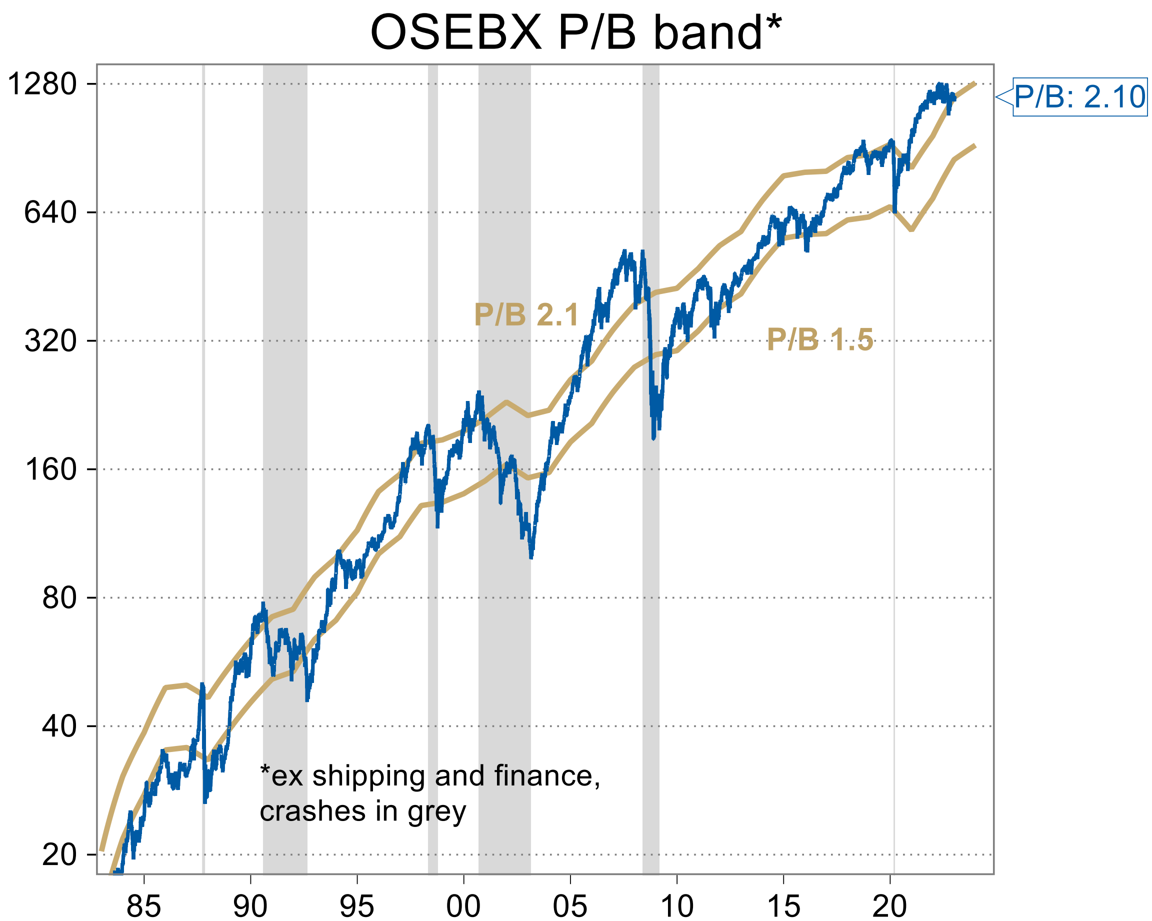
S&P up 2.4%, almost up to 4.000, the 10 y bond yield down 6 bp to 3.49%



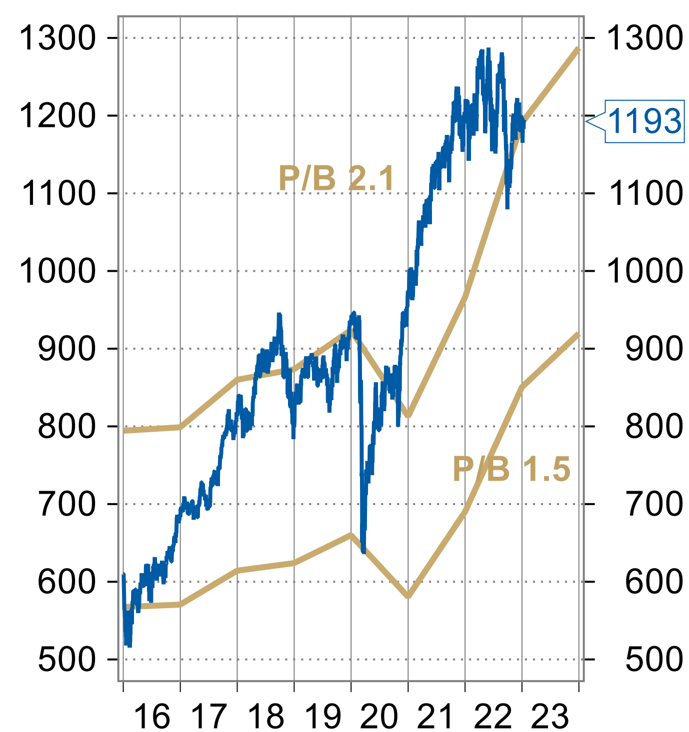


The OSEBX marginally down, with the oil price. The P/B is still high at 2.09

The book value is growing rapidly, due to the extremely strong energy sector earnings. But for how long??



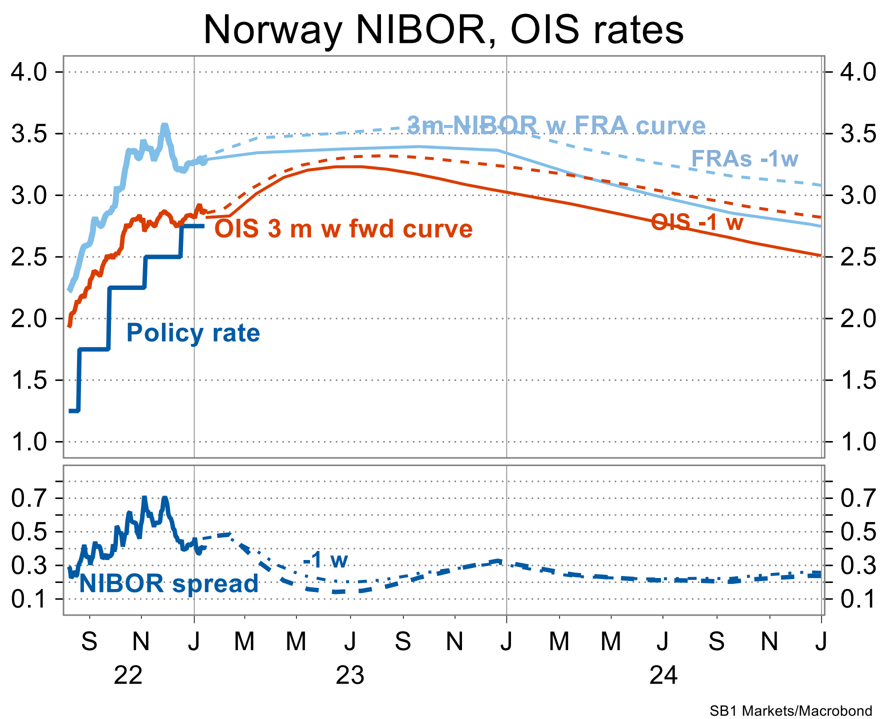
Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

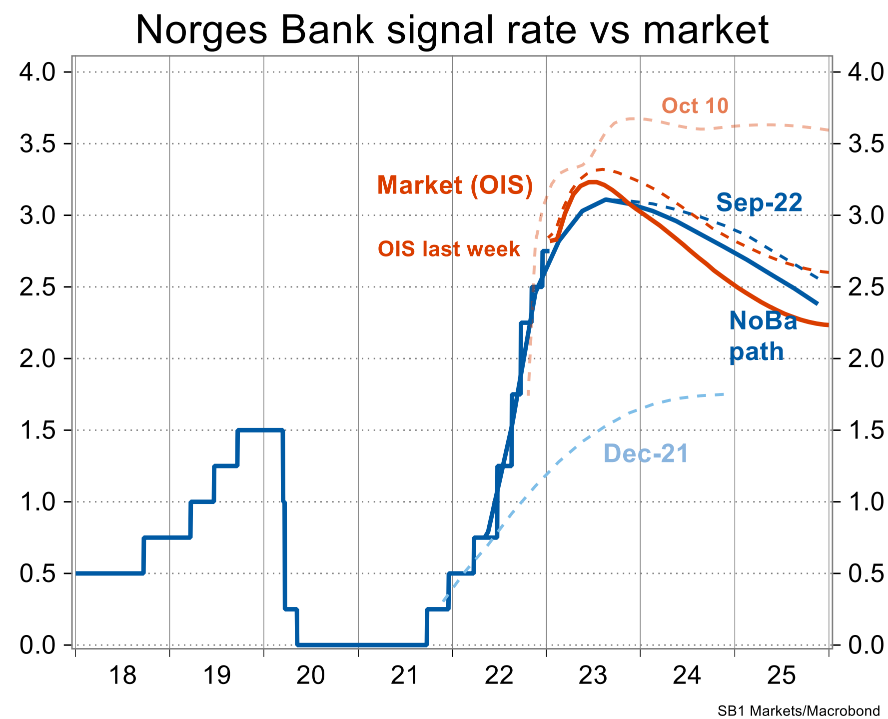


Source: Oslo Børs, Vital, Bloomberg, SB1 Markets, Macrobond.

Up & down again: The OIS curve shifted downwards last week

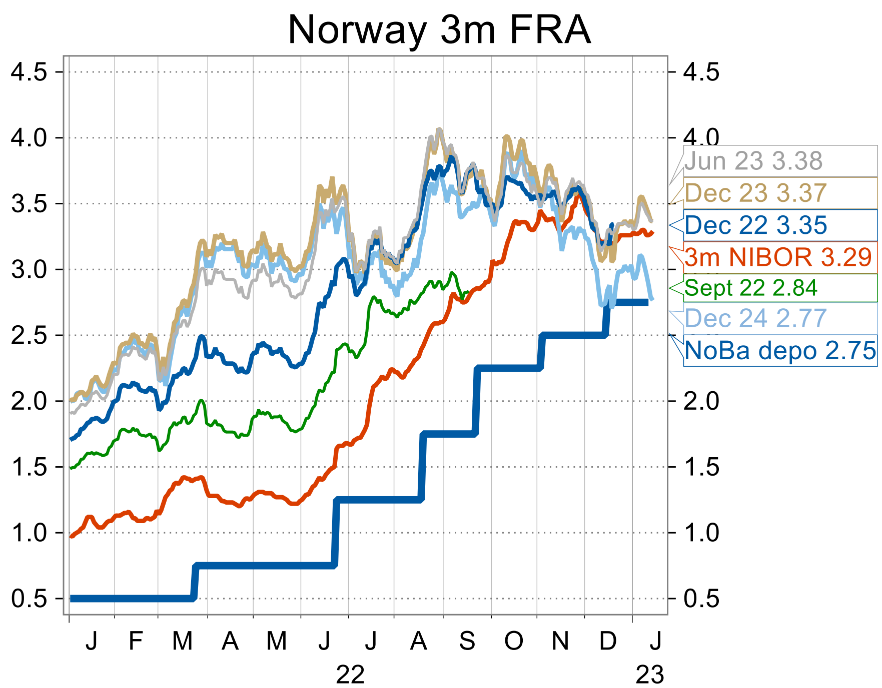
The peak was lowered by 8 bps to 3.23% (still two more hikes) but far more further out, by almost 40 bps from 2024



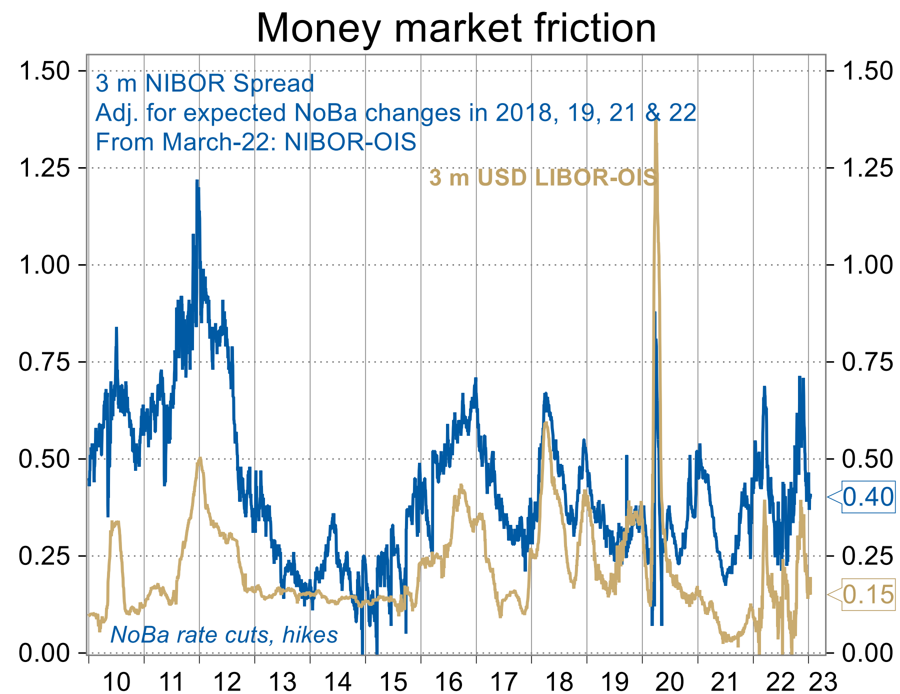


The NIBOR spread has almost normalised, now at 40 bps

FRA rates more than reversed the lift the previous week – but are still higher than in mid December



SB1 Markets/Macrobond



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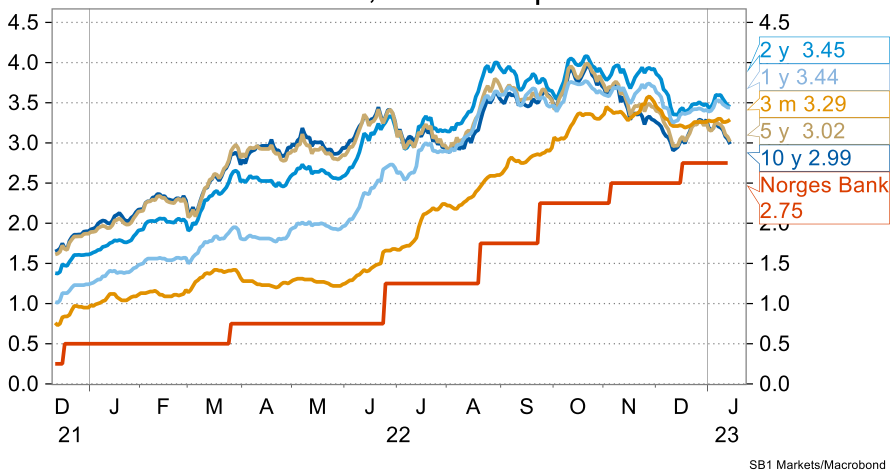
The whole curve down – cuts are expected

The 3m NIBOR has stabilised where it should be, at 3.30%

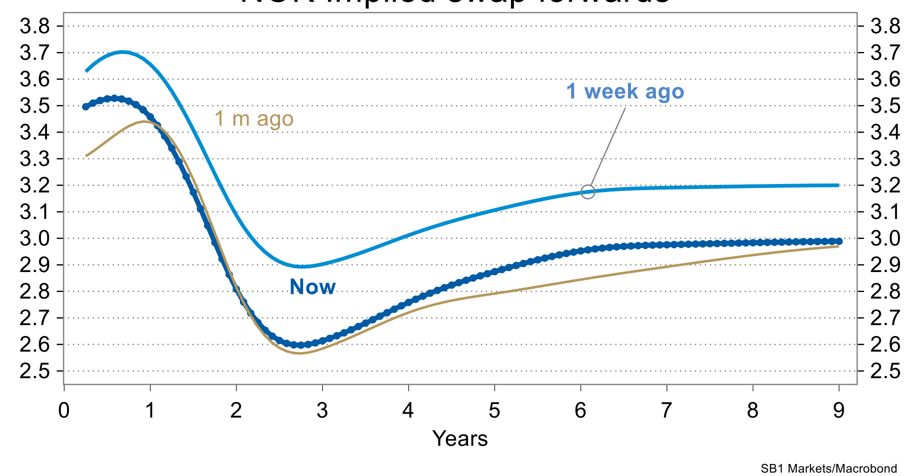
NIBOR, NOK swap rates



NOK Swap rates

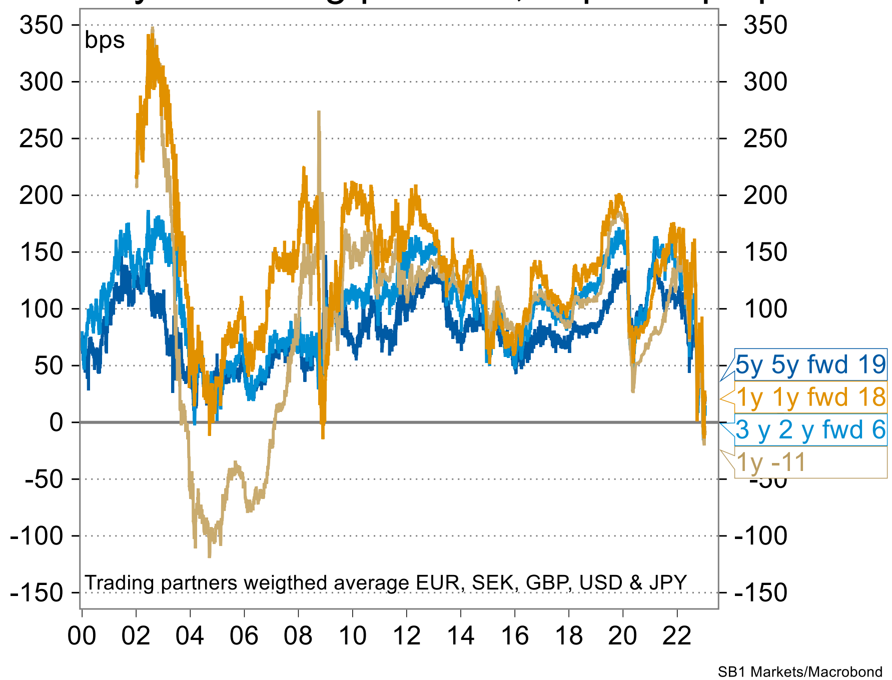
Norway - yield spread, 10y - 2y swap

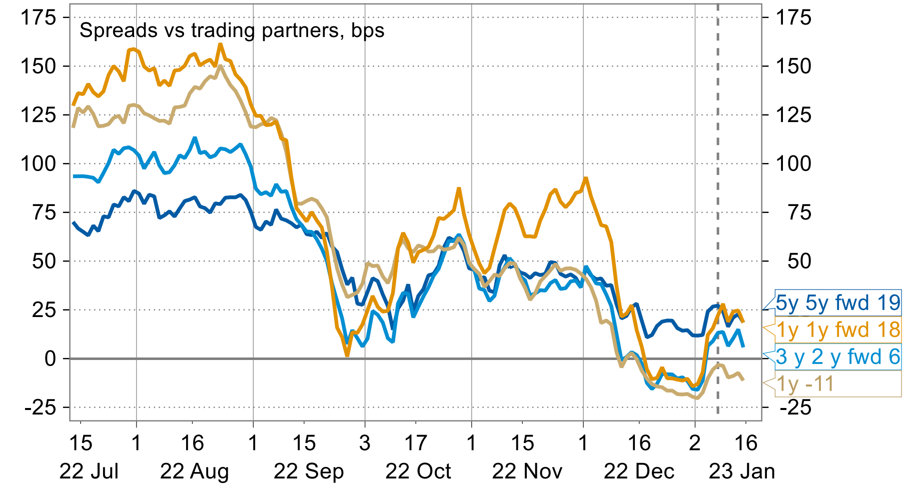
NOK Implied swap forwards



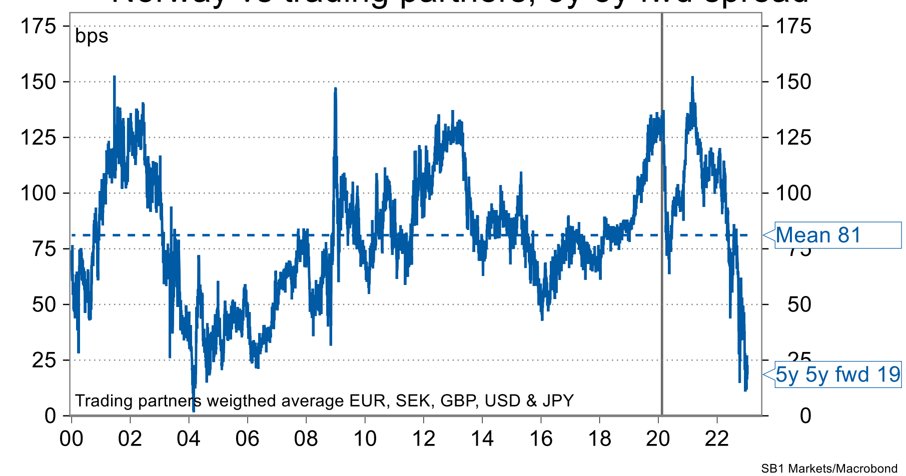
Spreads marginally down – and they are on the low side

Norway vs trading partners, impl swap spreads





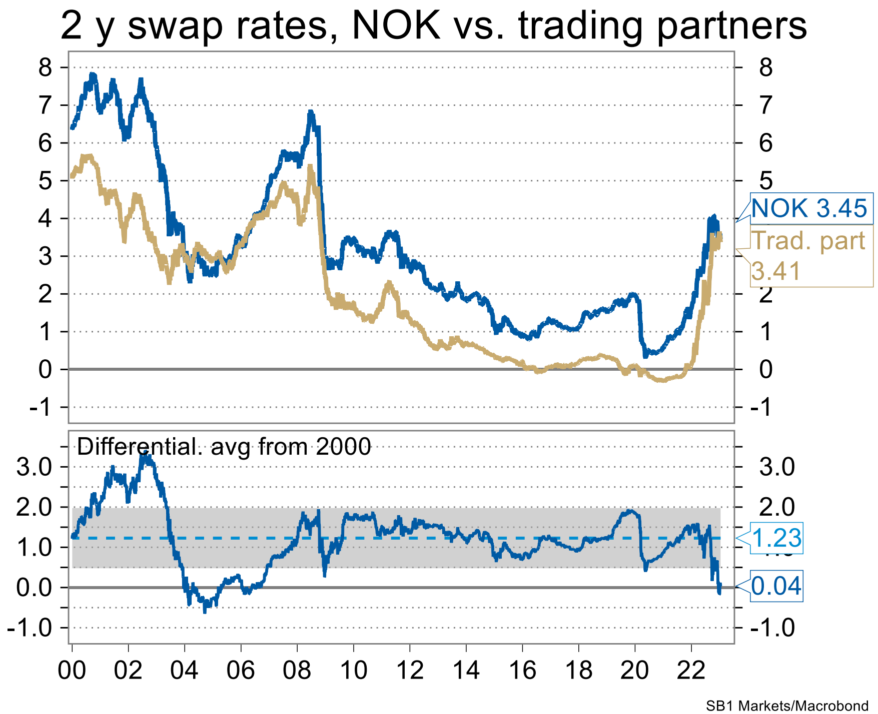
Norway vs trading partners, 5y 5y fwd spread

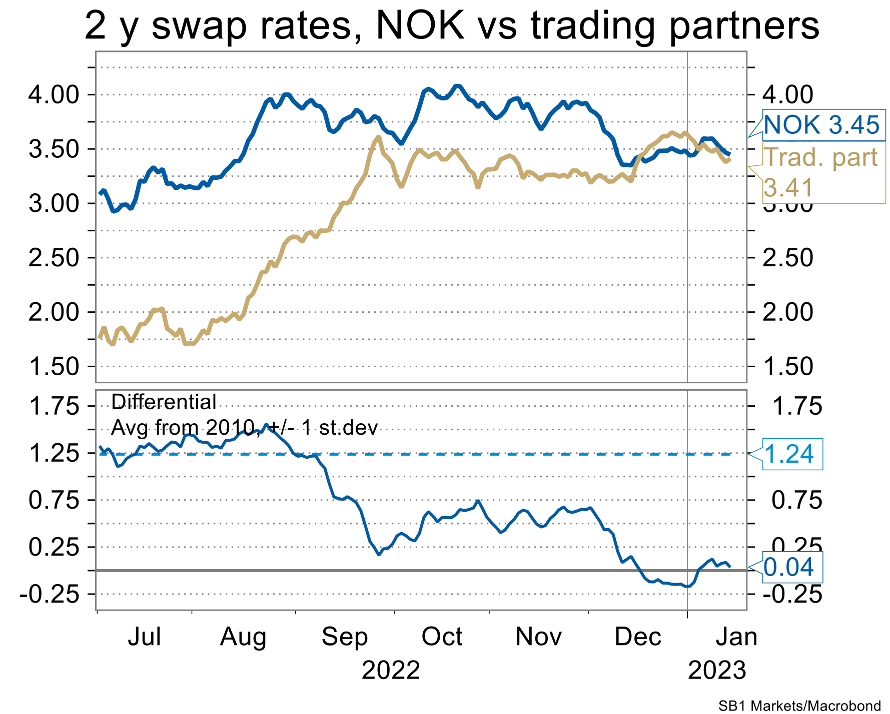


- Spreads were too wide, <u>now it may be too narrow</u>
  - **Norwegian inflation** has not been lower than abroad – and we doubt it will
  - **Higher oil investments** will give the Norwegian an idiosyncratic support the 2 – 3 coming years
  - The room for **fiscal expansion** is much larger than in any other country, if needed
- The 'only' risk: A collapse on the Norwegian housing market

The spread vs. trading partners at zero, the lowest since 2007

Since last August, the spread has narrowed by 170 bps, mostly due to the steep lift in rate expectations abroad

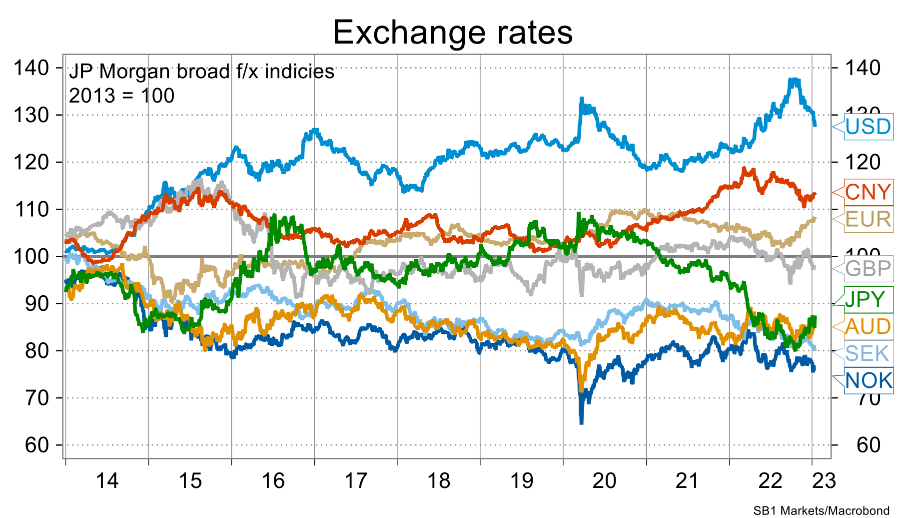


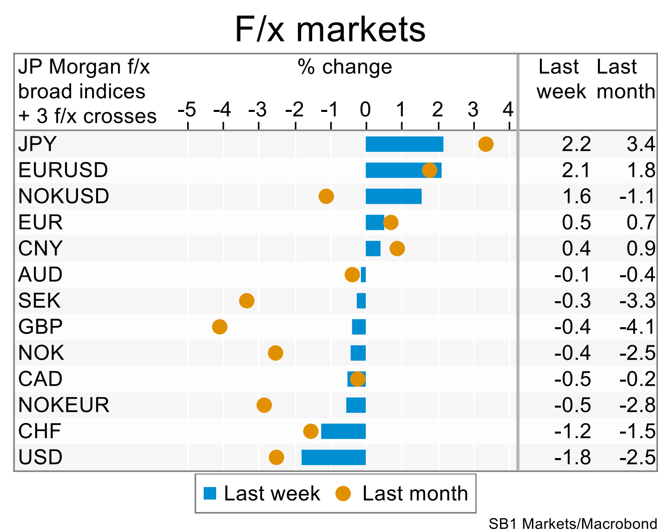


- See the comment on the previous page

JPY the winner last week, closer to a hike? And EUR further up, USD down

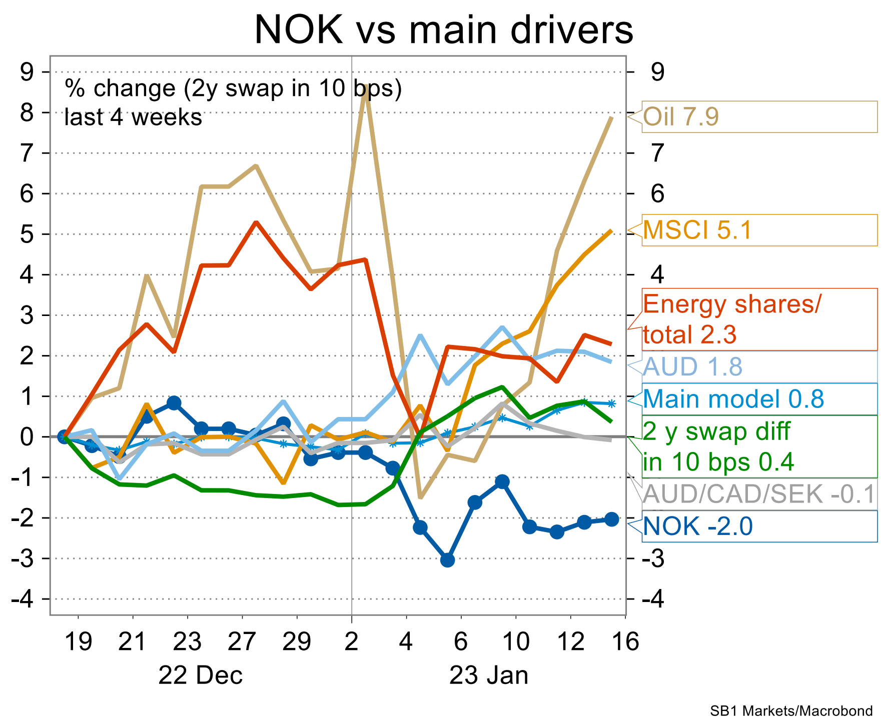
NOK marginally down, even if most arguments favoured the NOK

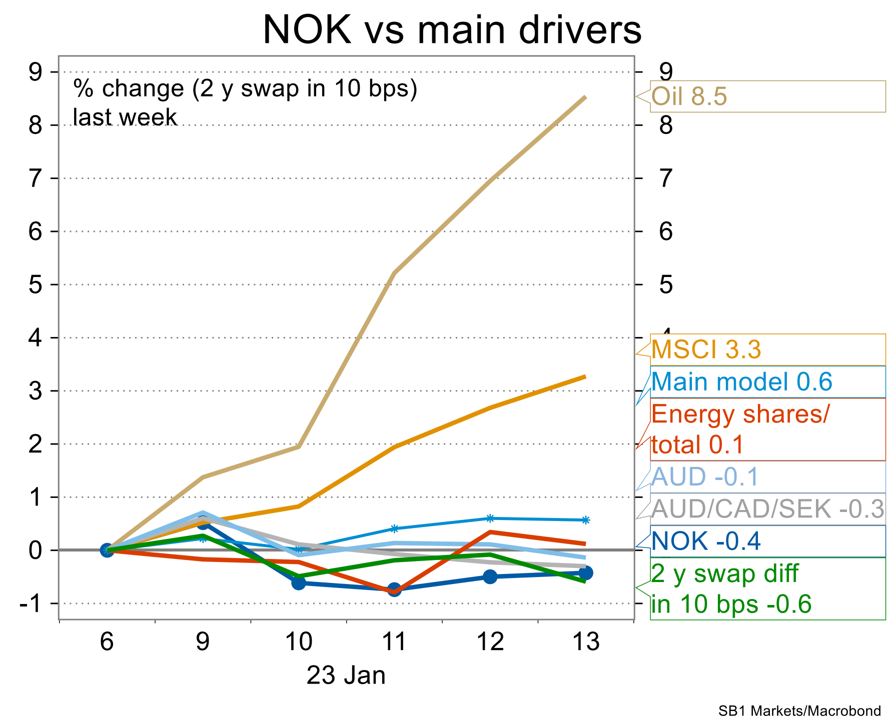




NOK down 0.4% in spite of risk on, a stronger oil price, and our model's +0.6%

(Is the huge decline in gas prices?). However, other raw material exporters did not appreciated the bull story either…

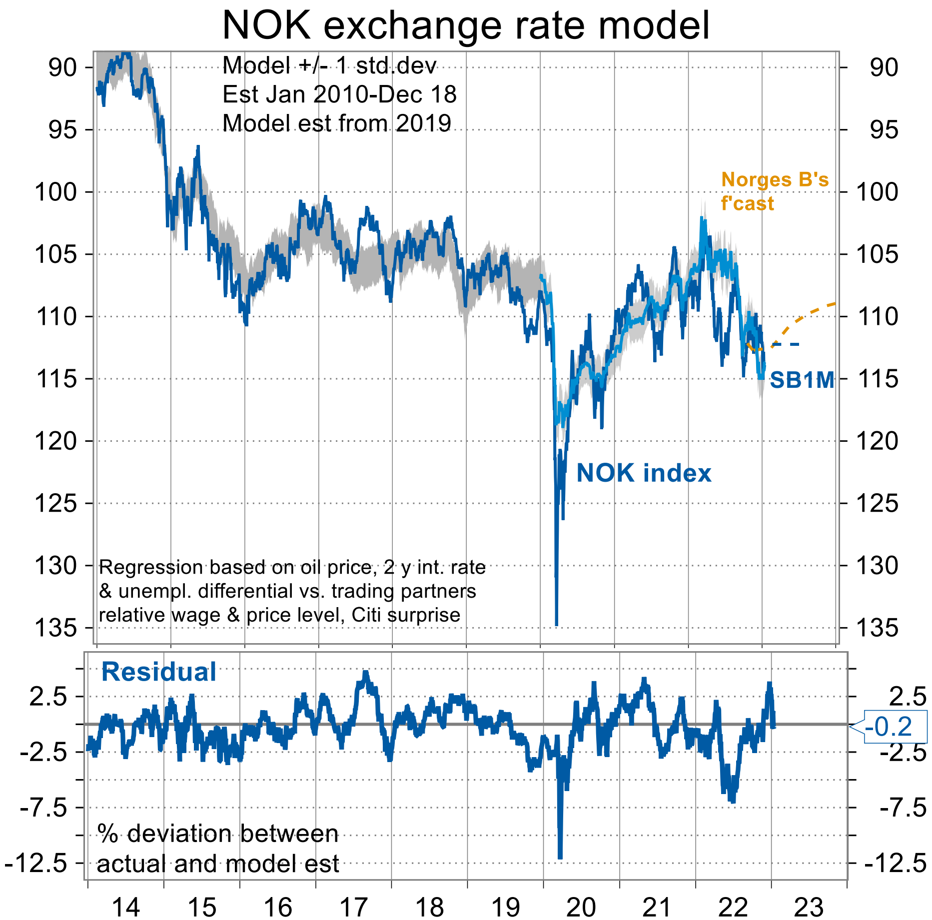


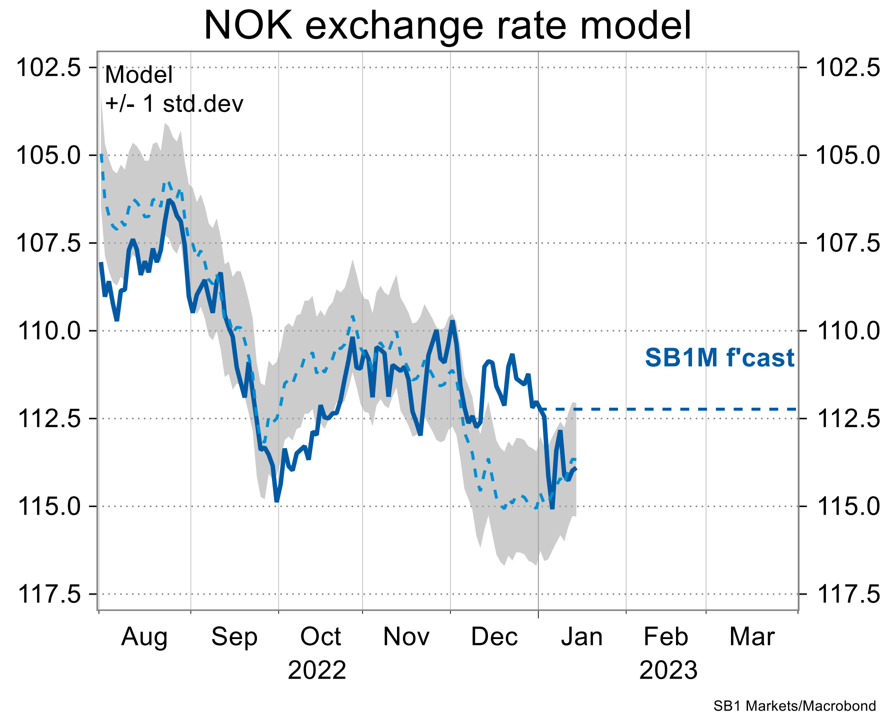


- NOK is 0.2% below our **main model estimate** (from +1.1%)
- The NOK is 7% weaker than our **AUD/CAD/SEK-model**, our 'super-cycle peers', predicts, a substantial weakening (from -9%)
- NOK is 2% weaker than an estimate from a model that includes global **energy companies' equity prices** (vs the global stock market) (from 4%)

On this and the following pages we have swapped Norges Bank's I44 index for JP Morgan's broad NOK index and rebased it to the current index value for the I44. The I44 has an earlier closing time than the 'official' closing time for f/x crosses. There are no substantial difference between these two indices over time, The 2 y swap rate differential is measured in 10 bps - that is, 1 equals 10 bps

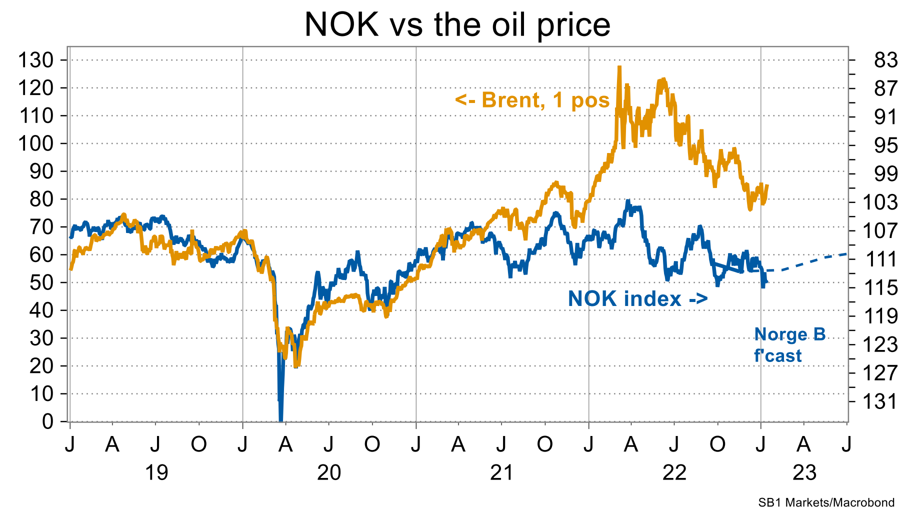
The NOK yielded 0.4%, while our model suggest at 0.6% stronger NOK

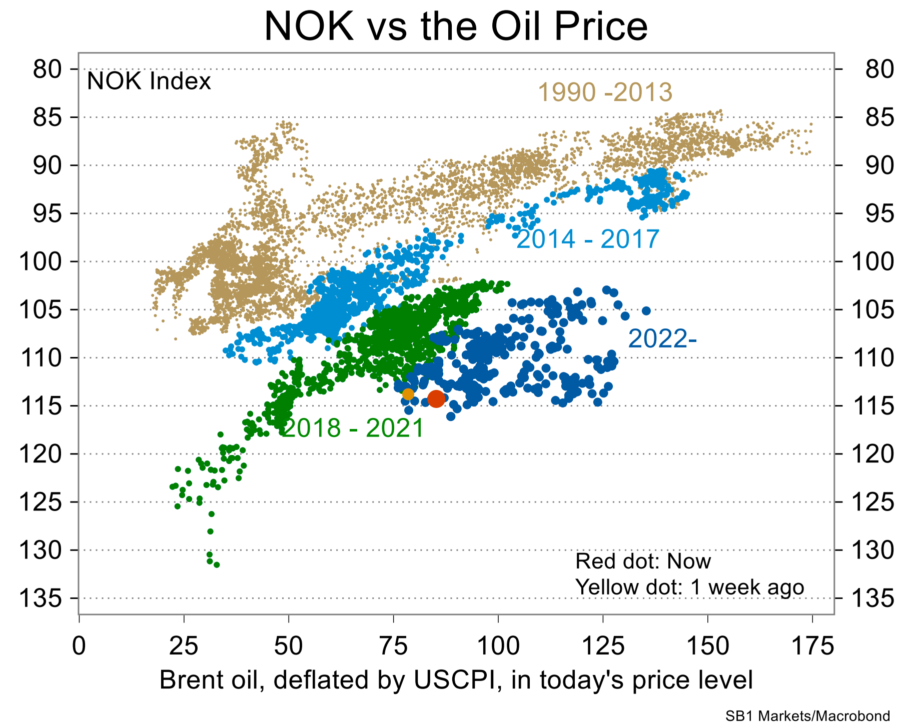


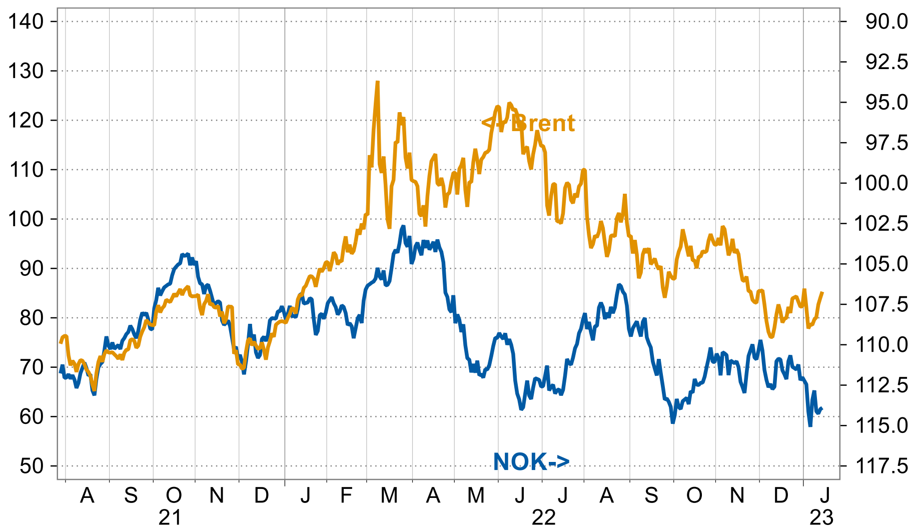


Oil up, NOK down

However, the NOK has been close to uncorrelated with the oil (or natural gas) price last year

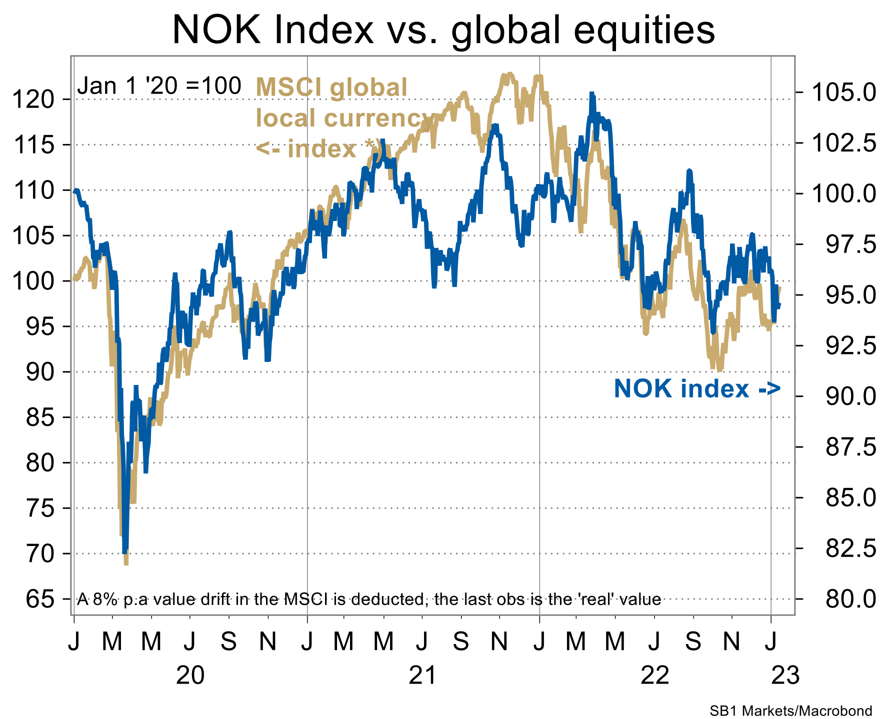


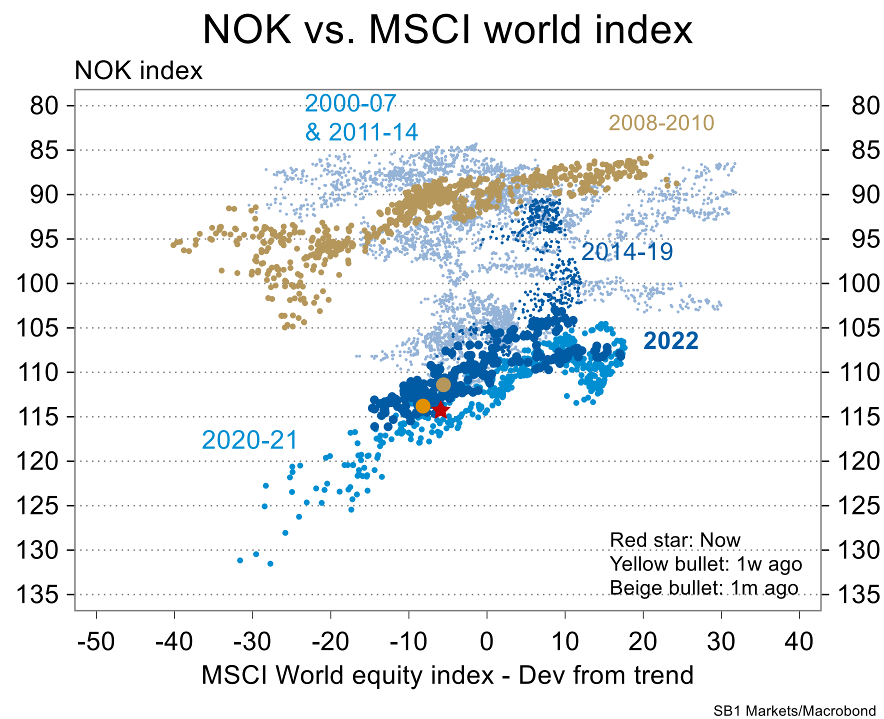




Global equities up, NOK down

The NOK has been closely in sync with the global stock market since April – but not so the recent weeks

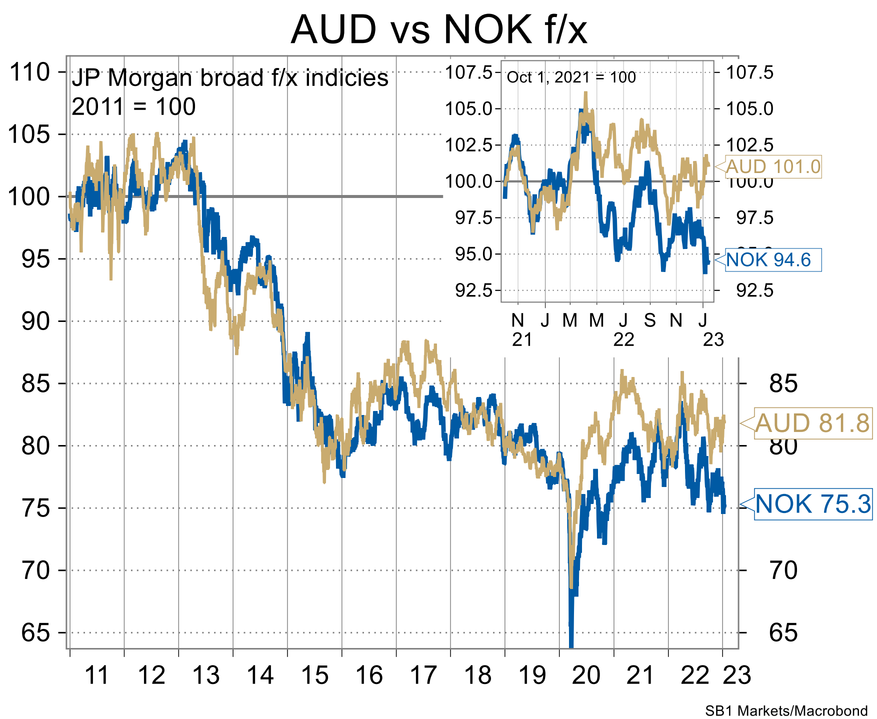


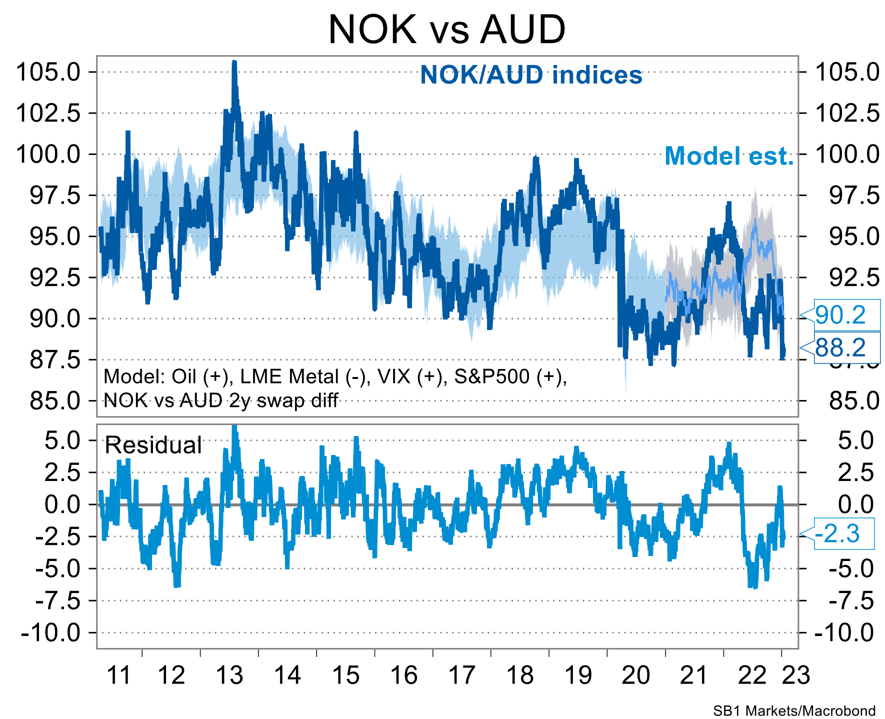


- There has not been any stable correlation over time, and when it is, the oil price is normally the real driver. *Not so much recent weeks*

The NOK/AUD gap close to unch. – and NOK is still on the weak side

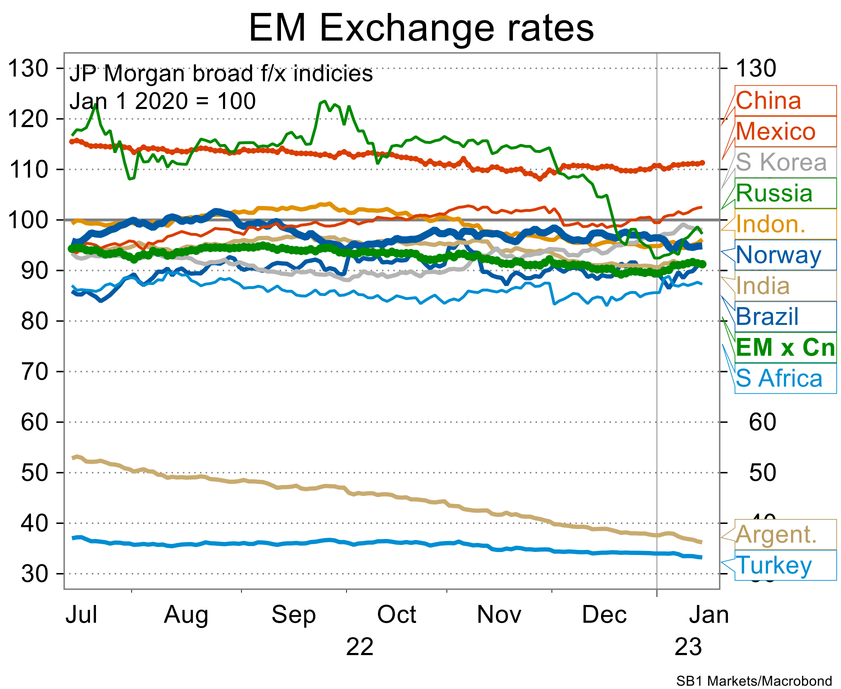
Higher metal prices and a lower oil price has until last week 'explained' a weak NOK vs the AUD

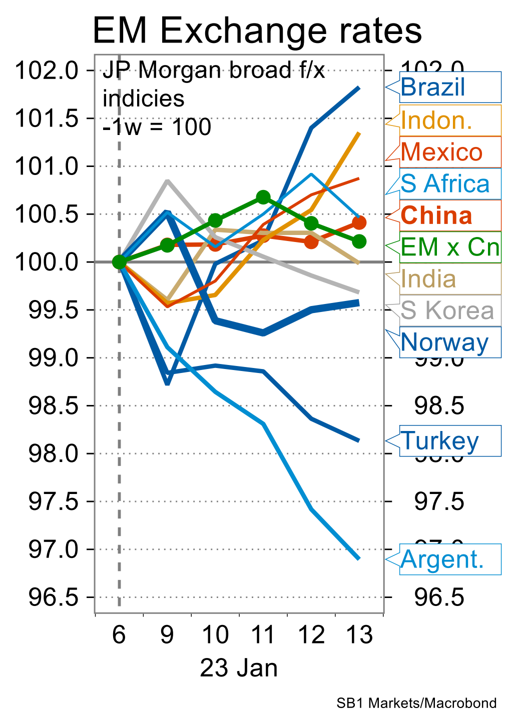


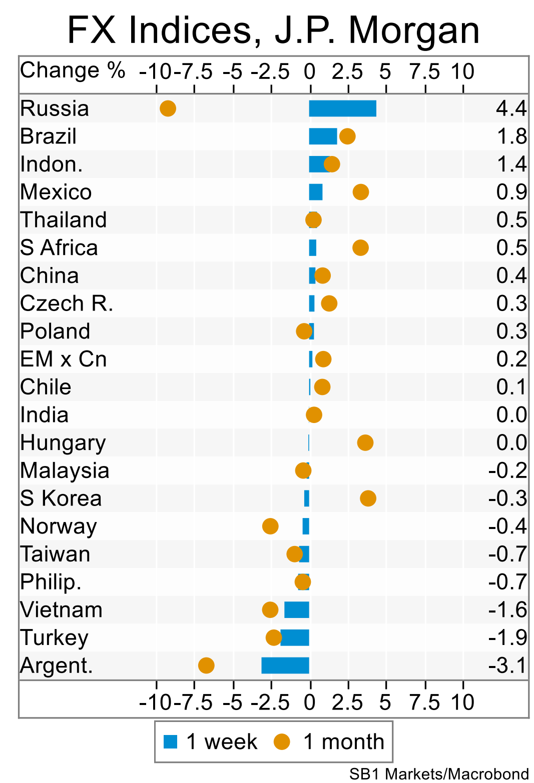


- Normally, NOK strengthens vs the AUD when the oil price rises vs. the LME metal index, when VIX, and the S&P500 index increases. The impact of interest rate differentials vs trading partners is added back to the model

Most EM f/x up, before the ‘good’ US news Friday afternoon







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